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1 See Vol. 3048  
**No. 15,640**

IN THE  
**United States Court of Appeals**  
**For the Ninth Circuit**

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JOHN PHILLIP ZANNARAS, J. P. ROBINSON,  
Jr. and U. S. TUNGSTEN CORPORATION,

*Appellants,*

vs.

BAGDAD COPPER CORPORATION,  
a corporation,

*Appellee.*

**APPELLANTS' REPLY BRIEF.**

---

JOHN PHILLIP ZANNARAS,  
J. P. ROBINSON, JR.,  
U. S. TUNGSTEN CORPORATION,  
P. O. Box 500, Congress, Arizona,  
*Appellants.*

**FILE**

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PAUL P. O'BRIEN, C



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JR. and U. S. TUNGSTEN CORPORATION,

*Appellants,*

VS.

BAGDAD COPPER CORPORATION,

a corporation,

*Appellee.*

---

**APPELLANTS' REPLY BRIEF.**

---

A great portion of appellee's brief is not open for review by this Appellate Court because as it was stated in appellants' opening brief (page 40) the controlling law in this case is the rule of the law of the case. Many issues discussed by appellee have been urged before on this Appellate Court, reviewed and disposed of.

We hold that all references in appellee's brief referring to the transcript of the affirmed case 321 consolidated for trial with case 221—*Bagdad v. Zannaras*, 229 F. 2d 920, and indicated by the number of said appeal, 14248 R, made for the purpose of defeating appellants' right are not reviewable by this Court.

We base our contention on the ruling of the following two cases from which we quote. *New York Life Insurance Co. v. Gamer*, 106 Fed. 2d 375:

“While affirmance of judgment must be considered adjudication by Appellate Court none of claims or errors are well founded, though all are not specifically referred to in opinion.”

Also in the case *Bennet v. City of Salem, Oregon*, 235 P. 2d 772 already quoted in appellants' brief (page 29) . . . that the estoppel must extend to every matter which might have been urged in case 321 to defeat the right, title or interest of Zannaras-Robinson.

Also on the principle that this Appellate Court has already reviewed this question.

Most of the second volume of this appeal which contains the expert testimony which is admitted in appellee's brief (page 27) is a relitigation of the deprivation of the Zannaras-Robinson water by Bagdad decided in Cause 321 Prescott while this case was pending on appeal before this Appellate Court by a perfected appeal No. 14248, is not before this Court for nonjurisdiction of the District Court.

As we pointed out in our opening brief (page 38) an appeal or error proceeding divests the trial Court of jurisdiction over matters necessarily involved in the review proceedings only (citing *White v. White*, 106 Pa. Super. Ct. 83, 161 A. 461). Vol. 3, *Am. Jur.*, Appeal and Error, Section 53, page 194.

We quote from *Rothchild & Co., et al. v. Marshall*, 51 Fed 2d 897,

“District Court is without jurisdiction of cause pending appeal from its judgment.”

On November 23, 1953, appellee filed a notice of appeal to this Appellate Court from the judgment of the Federal Court of the District of Arizona, entered against it in civil cause 321 Prescott (14248 R 43) and expressly presented to this Court in its assignments of errors and points to be relied on on appeal, the following:

That the District Court erred in ruling that for approximately five (5) months in each year due to appellant's (Bagdad's) pumping operations and use of water there was no water at appellees' (Zannaras-Robinson) point of diversion (14248 R 434) and also, that the District Court erred that appellant's use interfered with use of appellees at their point of diversion (14248 R 435).

According to appellee's brief (p. 27) on March 9, 1954, appellee was relitigating in the same District Court the same questions of the deprivation of the Zannaras-Robinson water by Bagdad on the same evidence already presented in cause 321 and pending then before this Appellate Court. In other words appellee was attempting to disprove in the District Court by expert opinion the findings established in cause 321 that for five (5) months there was no water at the Zannaras-Robinson diversion point due to Bagdad's use above, and simultaneously was urging on both Courts, Appellate and District, the *Albion-Idaho Land Company v. NAF Irrigation Company*, 97 Federal 2d page 439 (R 350) as a case to support its point of view.

The District Court having no jurisdiction to relitigate an issue pending before the Appellate Court it appears

that all the expert testimony in the last volume is not before this Court of Appeal, for lack of jurisdiction of the District Court on this question.

Appellee is basing its claim that actually case 221 was relitigated in the hearing of March 9, 1954, because appellants' counsel made no objections that this evidence was improperly admitted (Appellee Brief, page 26).

In the first place counsel for the appellants was under the impression that the evidence introduced was according to the scope and object for which the hearing was held to determine the character of judgment to be entered against appellee, and this is clearly shown in page 1 and page 5 of the memorandum submitted by appellants to the District Court for this hearing on June 4, 1954, in which it stated "We consider the entire testimony entirely unrelated to the subject matter of this hearing" and on page 10 they pleaded their adjudicated water right from Cause 321.

This memorandum as well as the memorandum of appellee for the same hearing, dated June 16, 1954, are before this Appellate Court as part of the record of this appeal. It can be seen from appellee's memorandum that in June 1954 appellee was urging at the same time the identical issues, on same evidence, with identical arguments, in two Courts, in the District Court, with memorandum and in the Appellate Court with his brief as appellant in case 321.

If our contention is right that the Court had no jurisdiction in the 1954 proceedings all appellee's references indicated in his brief from R 347 to R 636 are not before this Appellate Court because this part of the record contains the above mentioned proceedings.

It follows that since the District Court was without jurisdiction in the proceedings of May 9, 1954, its findings of fact, conclusions of law and judgment of April 17, 1957 which were deduced from the above mentioned proceedings are null and void on the face of the record.

---

### **CONSOLIDATION FOR TRIAL.**

Appellee represents to this Court that cases 321 and 221 were not consolidated for trial (Appellee Brief, pages 27-28).

The fact whether or not cases 321 and 221 were consolidated for trial is shown on the face of record. At the beginning of the 1952 trial on May 13 the Clerk of the Court in announcing the cases before the Court stated:

The Clerk. Civil 221. Prescott, John Phillip Zannaras and J. P. Robinson, Jr., v. Bagdad Copper Corporation, and plaintiff's amended Petition for Relief for hearing 321 Prescott Bagdad Copper Corporation, a corporation, v. John Phillip Zannaras, et al., for trial (14248 R 51-52).

Zannaras-Robinson had pleaded in both 221 (R 5) and 321 (14248 R 11) deprivation of water by Bagdad. This alleged fact was common to both cases and the evidence, adduced to support this fact, was common to both cases.

Bagdad had with words distinct and sufficient connected the pleadings of cause 221 and 321 (R 22-23). Both cases 321 and 221 had common points of law, that is, the validity of Zannaras-Robinson water right. The evidence of the deprivation of Zannaras-Robinson water is spread throughout the entire transcript.

The judgment rendered on cause 321 was deduced from the entire record, not from a certain number of pages.

At the beginning of the trial in 1952 Bagdad stated:

“Mr. Wilmer. In the interest of saving time I desire to go along with the business of trying the cases together but I do feel that we should attempt insofar as possible to separate them because in the event one should go up and the other does not.

The Court. Why not consolidate? It is all the same issue.” (14248 R 52).

It is apparent that if the issue was the same as the Court stated, Bagdad’s opinion or expectation that if one case should go up and the other does not . . . was incorrect because for the same issue it was impossible to have two contradictory judgments.

If cause 321 determining the validity of the Zannaras-Robinson water rights was lost to Zannaras-Robinson, case 221 in which Zannaras-Robinson were asking injunctive relief and damages would have been dismissed.

If cause 321 was decided in favor of Zannaras-Robinson case 221 would have been automatically lost to Bagdad, because the Court had to protect the Zannaras-Robinson water rights by an injunction against Bagdad. This point is explained in Kinney on Irrigation and Water Rights Second Edition Vol. 3 P. 12628, page 2974.

“INJUNCTIONS TO PROTECT DECREED RIGHTS. Although the rights of the respective parties to the use of waters from the same source of supply may be adjudicated and as so adjudicated may be protected by injunction granted in the same action, this is not always done.

Where, however, the rights have been adjudicated in previous action, and the decree is in full force and effect an injunction in a subsequent action will always be granted in a proper case to prevent interference with rights decreed by the parties to the previous action. Such an action is to protect priorities already established and not to determine them." Citing *Medano D. Co. v. Adams*, 29 Colo. 317, 68 Pac. Rep. 1958.

It is therefore apparent that the Court was right when it stated it is all the same issue and Bagdad had a misconception that one case can go up and the other may go down.

It clearly appears from the record that case 221, the amended petition for relief, and case 321, were placed, by the Court, on the same hearing by the Court's discretion. They had common points of fact and law which appear throughout the entire record.

Bagdad wished to attempt insofar as possible to separate them, but this was not done, and could not have been done, on account of common points of fact and law.

It appears, therefore, that cases 321 and 221 were consolidated for trial as it has been stated by appellants.

---

#### **APPEALABILITY OF THE 1951 JUDGMENT.**

Appellee states in its brief (page 2) that the 1951 judgment adverse to appellants from which no appeal was taken and which has long reposed undisturbed . . .

By this statement appellee attempts to convince this Appellate Court that the interlocutory decree of the 1949

trial is not appealable because an appeal should have been taken in 1951 when the interlocutory decree was issued by the Court.

Bagdad is in error because the appealability of a decree is determined by the finality of the decree. We quote from *Hunter v. Federal Life Ins. Co.*, 103 F. 2d 192:

“Judgment or decree, to be reviewable, must be not only final, but complete, that is, final not only as to all parties, but as to whole subject matter and all causes of action involved, and if not complete, appeal must be dismissed.”

Also, we quote from: *Western Union Telegraph Co. v. United States & Mexican Trust Co., et al.*, 221 Fed. 545.

“At the entry of the final order or decree in equity all the proceedings, interlocutory orders and decrees relative to the matters in controversy between the parties in interest therein are subject to revision by the Court entering the final order or decree, and on an appeal therefrom they are reviewable by the Appellate Court and may be heard at the same times.”

It is unquestionable that the interlocutory decree of the 1949 trial when the Court kept cause 221 under its jurisdiction could not be appealed at the time of entry of the judgment in 1951 and it is appealable now with the final disposition of cause No. 221 and should be reversed.

The entire first volume of this appeal and part of the second volume constitute the transcript of the 1949 trial; at the beginning of the 1952 trial on May 1952 the Clerk of Court in announcing the cases stated:

“The Clerk. Civil 221 Prescott, John Phillip Zannaras and J. P. Robinson, Jr., v. Bagdad Copper Cor-



poration and plaintiff's amended petition for relief for hearing 321 Prescott, Bagdad Copper Corporation, a corporation, v. John Phillip Zannaras, et al., for trial (14248 R 51-52)."

The above clearly shows that case 221 was before the Court for trial in the 1952 hearing and the judgment of the 1949 trial was not final judgment for cause 221 Prescott.

At the beginning of the 1952 trial counsel for appellant stated:

"Mr. Morgan. We desire as far as possible not to refer back to that, because as counsel said, in the case of appeal there is no use going back in the original record. I imagine.

The Court. There is no original record. We are still trying 221. The Court held in abeyance (14248 R-55)".

The judgment of the 1951 trial (R 12) was erroneous and must be reversed.

At that trial Zannaras-Robinson offered their water right in evidence without objection from Bagdad (R 101). In the following case it is shown that failure to object when a water right is introduced in evidence constitutes a prima facie case of the truth of the water right. *Water Rights of Owyhee River*, 124 Ore. 44, 259 Pac. 292.

The Court found in the 1952 trial that Bagdad had actual and constructive notice of the issuance of Zannaras-Robinson water right on January 2, 1945 (14248 R 39).

Bagdad consented to judgment against it on July 21, 1945, in which judgment it consented that Zannaras-Rob-

inson was lawfully using the water of Burro Creek (14248 R 432).

This case was before the same Court and brought by Bagdad to the judicial notice of the Court by introducing evidence from case 129 in the 1949 trial (R 327-329).

Bagdad admitted in its pleadings of cause 321 that Bagdad in the 1949 trial was not permitted to question the validity of the Zannaras-Robinson water rights (14248 R 8-9).

Zannaras-Robinson having established a prima facie case it was upon Bagdad to prove by clear and convincing evidence that it did not interfere with the Zannaras-Robinson vested rights. The Court erred in placing the burden of proof on Zannaras-Robinson. This subject is dealt with extensively in appellant's brief under Burden of Proof, page 19.

It is clear that the findings do not support the judgment and this being an error at law in an equity case it is open for review by this Appellate Court under all circumstances.

---

#### **REPLY TO STATEMENT RE JURISDICTION.**

Appellee states:

“Neither the District Court nor this Court on appeal in case 321 determined the same water rights” as are involved here (page 2).

The record clearly shows that the Zannaras-Robinson water right No. 1341 admitted in evidence as Exhibit No. 1 (R 101) in the 1949 trial of case 221 and is before this

Appellate Court (R 652). The same Zannaras-Robinson water right No. 1341 was introduced in evidence as Exhibit A (14248 R 22) in the 1952 trial of the consolidated for trial cases 221 and 321.

Bagdad's water right certificate No. 1314 was introduced as Exhibit L-1 in the 1949 trial of case 221 (R 324) and again as Exhibit J (14248 R 397) in the 1952 trial of the consolidated for trial cases 221 and 321.

Both water rights of appellants and appellees are clearly identified by number, amount of water and dates of priority in the findings of fact (14248 R 38) of case 321, affirmed by this Court (229 F. 2d 920). Appellee (Bagdad) makes no further statement to distinctly point out by the record that different water rights are involved in causes 221 and 321. It therefore appears that this statement of the appellee is entirely unfounded.

Appellee states:

“Practically the entire second volume of the Transcript of Record is made up of evidence, taken long after cause 321 was submitted to and decided by the District Judge.”

According to counsel's admission appearing on the record the entire second volume is not evidence but computations. He states, addressing the Court:

“We will show you by computations that . . .”  
(R 354)

and as we have demonstrated in appellant's brief (pages 66-67) these computations are contradicted by all Bagdad witnesses who testified to the facts predicted by those computations.

**INCONSISTENT STATEMENTS OF APPELLEE.**

Appellee has scattered through its reply brief certain attacks on appellants as to the real intentions of appellants' attempting to represent to this Court that the present case on appeal is a "hold up" case, notwithstanding the fact that the record shows that appellants have spent \$250,000.00 in their properties (14248 R 352).

Although we feel that it would have been unnecessary to give reply to them, however, we will point out to this Appellate Court the inconsistency of these attacks and innuendoes. Appellee states in its brief (page 22) that Zannaras knew that the creek historically dried up . . . and quotes Zannaras: "I have known that there are seasons of the year when there is no running water to be seen in Burro Creek" (14248 R. 411). We give below the full statement of Zannaras from which the above fragment is taken, from a deposition taken on the 2nd of July, 1945, prior to the pollution trial case 129 Prescott (14248 R. 400):

"Q. As I understand it Burro Creek is a running stream?

A. Yes, continuous.

Q. How much water does it carry?

A. Well, in a dry season it carries very little.

Q. If I went out there today, how much water would there be running down the creek there?

A. Well, there is now, right today, there is enough water, but in the drier season——

Q. How wide a stream?

A. I should say the stream runs in places about ten inches wide and about three inches deep.

Q. And then of course when it gets there is rain or other water, it runs pretty high some time?

A. It is getting much less water. I have known that there are seasons of the year when there is no running water to be seen in Burro Creek." (14248 R. 411).

The above testimony made in July 2, 1945, clearly shows that Zannaras stated that Burro Creek is a continuous running creek. In fact the same was the understanding of the counsel as it is shown from the question he made.

If Burro Creek was a dry creek for five months at the Zannaras-Robinson point of diversion as it is shown by the affirmed judgment of this Court the counsel could never have made such question.

"As I understand it Burro Creek is a running stream", and he should have resisted Zannaras' answer: "Yes, continuous", which clearly shows that the flow of the creek was not intermittent.

The Zannaras testimony is in complete agreement with other testimony and especially with the testimony of Mr. Albert Austin (14248 R 122) postmaster at Congress who was the only witness who lived at the Zannaras-Robinson place from 1933 to 1936 (14248 R 121).

It also agrees that in a dry season at certain points the creek flows under sand and gravel and emerges when the bed of the creek is solid rock (14248 R 127). Appellee states in his reply brief (page 22)—quoting Mr. Zannaras: "No, this time today we have a very dry spell along there; it is now dry this time." (14248 R 390).

The above is also a fragment from Bagdad's Exhibit G which is part of the transcript of the pollution case 129

Prescott (14248 R 374). This testimony was taken on July 21, 1945. We quote the statement from which this fragment was taken:

“Mr. Wilmer. Mr. Zannaras, referring to these pictures identified as plaintiff’s Exhibit G. These pictures were taken when Burro Creek was rising or running more than ordinary, were they not?

A. No.

Q. You mean you now state to the Court today that these pictures represent Burro Creek in its normal flow?

A. I don’t know what you mean by normal flow.

Q. Like its normal flow?

A. Now there is very little water running through. There was some water going through at that time.

Q. Is it not a fact that these pictures do not represent Burro Creek as you saw it, the biggest part, throughout the year?

A. No. This time today we have a very dry spell along there; it is now dry this time of the year” (14248 R 390).

The above testimony clearly shows that on July 21, 1945, Zannaras testified that there was very little water running through. Nineteen days before July 2nd, he testified that the width flow of the creek was ten inches wide by three inches deep (14248 R 411).

The last statement, dry spell, etc., refers to the weather and not to the water in the creek.

Appellee in its brief (page 22) attempts to represent that Zannaras-Robinson picked a diversion point where the gravel is thick so there will be not water flowing in order to create trouble for appellee.

Mr. Sherman Decker of the U. S. Geologic Survey Surface Water Division an entirely impartial witness testified that the Zannaras-Robinson diversion point is in solid rock (14248 R 129). Mr. C. H. W. Smith, Engineer of the Water Commissioner of the State of Arizona testified that Zannaras-Robinson point of diversion is on rock (14248 R 118). Mr. Albert Austin, Postmaster at Congress, testified the same thing (14248 R 127).

Appellee repeatedly states in its reply brief that Zannaras-Robinson refused to work their mill. Appellants in their pleading specifically plead that it is impossible to work economically without their water (R 14, R 5, 14248 R 12). We quote from the record:

“Q. What I am curious to know Mr. Zannaras is why, when there is no opportunity to run your mill, you don’t make any effort to get ready to run it when the time comes to run it.

A. All right, let me answer it. The conditions you fellows have created for me up there makes it impossible for anyone to work under those conditions. What do you want me to do?” (14248 R 103).

Bagdad stated in their pleadings of cause 321 (14248 R 5) and in the opening brief of cause 321 (page 2) to this Appellate Court that without the Zannaras-Robinson water they will have to close down, yet they do insist that appellants should work without water intermittently and uneconomically which they themselves cannot do.

Appellee admits there are water problems for all and it tried to solve them by building a dam. However, it states that appellants prevented it because appellants filed a protest and also filed a right of way near the place of

its damsite, which for some unexplained reason made appellee quit its original damsite to a new damsite one mile down stream. Appellee fails to show why it did not build the dam in the new location to solve everybody's water problems. This testimony appears on (R 611, 612, 596, 597).

The above testimony is given by Mr. Dickie the General Manager of Bagdad who continues on page 614. He is asked the following question:

“Q. You hope to find a well perhaps, that would give you that supply, in the event Mr. Zannaras' position is finally sustained, is that correct?

A. Yes.”

This testimony was taken on March 11, 1954, while the Zannaras-Robinson water right was on appeal.

The General Manager of Bagdad admits that if the Zannaras-Robinson water rights are sustained by the Appellate Court he must have a well to give him the supply he is now taking from the Zannaras-Robinson water rights.

The Zannaras-Robinson water rights were sustained and affirmed on January 30, 1956.

There is nothing in the record to show what happened to the well.

More than a year after the issuance of the Mandate of this Appellate Court, ordering the Zannaras-Robinson were entitled to waters of Burro Creek without interference from Bagdad.

The District Court, by this judgment in April, 1957, reversed and impeached the judgment of this Appellate



Court and in effect cancelled the priority and the Zannaras-Robinson water rights.

Appellee in its reply brief (page 12) as well as in its brief of case 321 (page 41) attempts to impress this Appellate Court of the importance of its operations to the economy of the State and the unimportance of the appellants' operations. We believe that the following quotation from *Morris v. Bean et al.*, 146 Fed. 423, will be of assistance to this Appellate Court in the understanding of appellant's case because the above case seems parallel and coincident to several points of the present appeal.

*Morris v. Bean et al.*, 146 Fed. 423.

“The appropriators took with the right to have the stream continue to flow as it was wont to flow, and to remain in the condition in which they found it, and whenever water is diverted above it keeps back that which would otherwise reach them, and the more water that is kept back the less will the complainant and intervenor have. But for the wholesale diversions by defendants the water would reach them later in the season and abide longer, and this is what their appropriations entitle them to. In the abstract there would be more people benefited by allowing the defendants to take all water. Its flow through a sandy and gravelly stretch of something like eight or ten miles, and perhaps farther, is in a measure, a waste, but equity does not consist in taking the property of a few for the benefit of the many, even though the general average of benefits would be greater. It can no more ignore well-defined legal rights than it can go in the face of a positive statute.

“Then again, the theory of the defendants cannot be accepted. The witnesses perhaps have told the

truth, but not the whole truth. That the water would not reach one lower down the stream is quite a common defense. It is often urged in irrigation suits by trespassers as a justification for their invasion of the rights of others.

“It is probably as old as irrigation and perhaps as trespass itself. In this case failure of the water to reach the complainant and intervenor was coincident with its use by the defendants. The fact that witnesses saw in the varying changes of the seasons a shortage of water at different points on the stream does not explain the whole situation: in other words, in one extremely dry season perhaps the water was lower than in another. It varies, and it varies because of the shortage of the supply above, and these defendants retarded its flow by reason of their diversions, which decreased the supply to that extent which prevented it from reaching Wyoming at all; and when the supply is diminished by the light snowfall the diversion of the defendants increases the shortage, and that is an invasion of the rights of the appropriators who are seeking the enforcement of their priorities in this suit.”

The Court then ruled as follows:

“The decree will enjoin the defendants from diverting the water of Sage and Pine Creeks to the prejudice of the parties found to be entitled to the same as prior appropriators the costs will follow the decree.”

### BURDEN OF PROOF.

Appellee states that the Court applied the rule based on the following principle:

A party who bases his right on prescription or adverse possession or abandonment or forfeiture of prior right has the burden of proof as to such matters, but, when he makes a prima facie showing the adverse party has the burden of rebutting to overcome it. 93 C.J.S. 1014, 1015, see 201—67 C.J. 1061, note 19.

The subject matter of the present case on appeal is shown affirmatively in the pleadings. Case 221 is not a question of adverse possession, or prescription. It is an interference with the prior vested rights of appellants due to numerous illegal acts by appellee. Bagdad's pleadings distinctly show that it is a straight denial of appellants' allegations (R 7-9; R 22-23).

In fact, in view of the ultimate theory of defense assumed by Bagdad, it was a requirement of the law that Bagdad should have made specific pleadings, which it did not. This subject is discussed by Kinney on Irrigation and Water Rights. Vol. 3, pages 1634, 2995.

“Where, also, the defendant relies upon the defense that the water if not diverted by him would be of no benefit to the plaintiff, for the reason that it would not reach him anyway, there is no question but that such a defense must be specially pleaded.”

#### Citing:

*Alamosa Creek C. Co. v. Nelson*, 42 Colo. 140, 93 Pac. Rep. 1112;

*Watts v. Spencer*, 51 Ore. 262, 94 Pac. Rep. 39;

*West Point Ir. Co. v. Moroni etc. Co.*, 21 Utah 229, 61 Pac. Rep. 16.

**ANSWER—RES JUDICATA.**

Appellee states in its brief:

“The Court by further minute order vacated the order taking cause No. 221 under submission specifically for the purpose of hearing further evidence.”

The record affirmatively shows that the evidence the Court wanted was for the purpose of determining the character of judgment to be entered against Bagdad (R. 23-25; R. 348).

Appellee further states:

“An order or judgment of the Court is not final . . .”

also

“Where two inconsistent judgments are rendered between the same parties the last in time controls.”

On January 30, 1956, this Appellate Court affirmed case 321. The effect of this affirmance was that the judgment in 321 became the judgment of the United States Court of Appeals, *United States v. Reid & Others*, 17 F. 497.

In *Bissell Carpet Sweeper Co. v. Goshen Sweeper Co.*, 72 Fed. 545, it is stated the decree and mandate of the Courts of Appeals have precisely the same finality as the decrees and mandates of the Supreme Court.

When the mandate of the United States Court of Appeals for the Ninth Circuit was entered in the District Court on March 12, 1956, the judgment of cause 321 had the finality of a decree of the Supreme Court of the United States.

We also quote from *City of Orlando v. Murphy*, 94 Fed. 2d 426. An affirmance on appeal is *res judicata* and no

power exists after the term to alter the decision and this is also true where the mandate requires the entry of specific judgment. This also is stated in *Seagraves v. Wallace*, 69 Fed. 2d 163.

On April 17, 1957, more than a year after the issuance of the Appellate Court's mandate, the District Court by its judgment reversed and impeached a judgment having a finality of a judgment of the Supreme Court of the United States on the same issue and evidence, namely, the deprivation of the Zannaras-Robinson water by Bagdad notwithstanding the fact that it was brought to the attention of the District Court by the appellants with strong and forceful representations that the District Court had no power, authority, jurisdiction or discretion to enter its judgment in defiance of the judgment of a higher Court as no power exists to change the decision of the Appellate Court after the term.

The District Court's persistent refusal to exercise its duty to follow what the higher Court decided resulted in the judgment of the District Court of April 17, 1957 being an error of law apparent on the face of the record.

As stated in our opening brief, page 39:

"Proceedings contrary to the mandate must be treated as null and void. \* \* \*"

Appellee further states, page 26:

Thirdly and conclusively:

". . . A sufficient answer is that neither by pleadings nor evidence were the proceedings in this other case brought before the court of claims in the present suit. If a party neither pleads nor proves what has been decided by a court of competent jurisdiction in

some other case between himself and his antagonist, he cannot insist upon the benefit of res judicata, and this although such prior judgment may have been rendered by the same court. . . .”

We stated in our opening brief (page 13) appellants pleaded the adjudication of case 321 before the District Court in their motion (R. 23-27).

Distinctly and sharply the decision of cause 321 was brought to the attention of the District Court by the following objections which are part of the record of this appeal:

“That the Findings of Fact proposed by the Defendant in Paragraphs 2-3-4 and 5 are wholly contrary to the Evidence before the Court and duly received by the Court in each of said causes of action, #221 and #321, which were consolidated for trial and Hearing.”

(Objections to the proposed Findings of Facts, page 2.)

“Plaintiffs further object to the Judgment proposed by defendant in said cause of action for the reason and upon the grounds that said Judgment proposed by Defendant is contrary to the Law and is in violation of Plaintiffs’ Rights as adjudicated by the Court in that cause of action entitled

Bagdad Copper Corporation, a corporation,  
Plaintiff,

vs.

John Phillip Zannaras, et al.,

Defendants.

cause of action #321, as shown by the Judgment of said cause of action with which this cause of action,

#221, was duly consolidated, as shown by the Records on file in these Proceedings.

*“Plaintiffs’ Objection #7*

“Plaintiffs further object to the Findings of Fact, Conclusions of Law, and Judgment as prepared by Defendant for the reason that the cause of Action #221 in the above entitled Court was duly consolidated with cause of action #321 in the above entitled Court, and that on November 12, 1953, this said Court in said cause of action, #321, duly entered its Findings of Fact, as follows, to-wit:

‘After the issuance of defendants’ certificate of water right, they used in their mining and milling operations and for domestic purposes, and put to beneficial use each year considerable quantities of water. For approximately five (5) months in each year, due mainly to plaintiff’s pumping operations and use of water above, there was no water at the defendants’ point of diversion.’

*“And that said Findings of Fact, Conclusions of Law, and Judgment entered by this Honorable Court on November 12, 1953, in cause #321 consolidated with cause #221, were duly affirmed on appeal by the United States Circuit Court of Appeals for the Ninth Circuit, and the fact that Defendant wrongfully and illegally took from Plaintiffs the water the use of which Plaintiffs were entitled to use and enjoy has been finally adjudicated and determined and is Res Judicata and this Honorable Court does not now have the power, discretion, jurisdiction or authority to adopt, approve, or enter the Findings of Fact, Conclusions of Law, and Judgment proposed by Defendant, and this Honorable Court has now only the power, jurisdiction and authority to enter judgment in favor of Plaintiffs and against Defendant, forever*

*prohibiting, debarring, and enjoining Defendant from taking from Plaintiffs the use of the water granted to Plaintiffs by the State of Arizona, by Certificate of Water Right 1341, dated January 2, 1945, with priority to such water from August 27, 1940, as set forth by this Honorable Court in its Findings of Fact dated November 12, 1953, in cause of action #321 consolidated with cause of action #221.*

*“Plaintiffs’ Objection #8*

“Plaintiffs further object to the Findings of Fact, Conclusion of Law, and Judgment as proposed by Defendant for the reason that the same are inaccurate, incomplete and erroneous in that said Findings of Fact, Conclusions of Law, and Judgment proposed by Defendant fail to show that Defendant’s appropriation of water was inferior to Plaintiffs’ Water Right, Certificate of Water Right #1341, and fail to show that Plaintiffs’ Water Right is prior in time and prior in right, and paramount, to any water right claimed, owned or possessed by Defendant, and said Findings of Fact and Conclusions of Law as proposed by Defendant fail to set forth the fact that Defendant did unlawfully and illegally change the diversion and manner of use of water and did unlawfully and illegally, annually extend the use of the water and did unlawfully and illegally appropriate 155,000,000 gallons of water annually in excess of the amount of water granted Defendant by the State of Arizona, by Certificate of Water Right 1314, and said Findings of Fact and Conclusions of Law proposed by Defendant fail to show that Plaintiffs’ Water Right is prior and paramount to the Water Right granted to Defendant by the State of Arizona, and said Findings of Fact and Conclusions of Law proposed by De-



fendant fail to show that Defendant deprived Plaintiffs, for a period of Five (5) months each year, or the use of the water granted Plaintiffs by the State of Arizona by Certificate of Water Right 1341.

*“Plaintiffs’ Objection #9*

*“Plaintiffs object to the Defendant’s proposed Findings of Fact, Conclusions of Law, and Judgment for the reason that the same are contrary to and in conflict with the Evidence before the Court in cause 321, consolidated with cause 221, upon which this Honorable Court based and predicated its Findings of Fact, Conclusions of Law, and Judgment, dated November 12, 1953, which said Judgment was duly affirmed on appeal by the United States Court of Appeals for the Ninth District and upon which Judgment on the Mandate so issued by said United States Court of Appeals for the Ninth District was duly entered in this Court on March 12, 1956, and the facts upon which this Honorable Court based and predicated its Findings of Fact, Conclusions of Law, and Judgment, dated November 12, 1953, in case 321 consolidated with cause 221, have been finally adjudicated and determined and are Res Judicata, and this Honorable Court does not now have the power, jurisdiction or authority to alter, amend or modify the Findings of Fact, Conclusions of Law and Judgment dated November 12, 1953, in said cause 321 consolidated with cause 221, by adopting, approving, signing or entering the Findings of Fact, Conclusions of Law, and Judgment as now proposed by Defendant and as now submitted to this Honorable Court by Defendant.”*

(These objections appear in the record in a separate document.)

It appears that appellants strongly and clearly called to the attention of the District Court that the deprivation of the Zannaras-Robinson water by Bagdad was *Res Judicata*, and that after the decision of the Circuit Court of Appeals that the District Court was limited in obeying the mandate.

In *Munro v. Post*, 102 F. 2d 686, it is stated that

“The phrase ‘Law of Case’ when used to express the lower Court’s duty to follow what higher Court has decided at an earlier stage of the case, applies to everything decided, either expressly or by necessary implication . . .”

It should be remembered that at the beginning of the 1952 trial when the cases were consolidated for trial it was the understanding that the Court would issue separate judgments for each case (14248 R. 51-54).

Upon affirmance of case 321 the District Court refused to exercise its jurisdiction to issue the judgment for 221 in compliance with the mandate of the Circuit Court and misconstrued and willfully disobeyed the mandate of the Circuit Court.

The effect of the judgment of the District Court is in effect delivery to the appellee of real property belonging to the appellants in defiance and contravention of the judgment and mandate of this Appellate Court having the finality of a judgment and order of the Supreme Court of the United States.

The District Court even failed to respect the constitutional rights of the appellants which they interposed in an

effort to stop the judgment, by specifically pleading in their objections to the Court.

On May 14, 1957, appellants filed a notice of appeal from the judgment entered in case 221 on April 17, 1957. ~~This notice which is part of the record in this appeal shows that it was served on Mr. Perry Ling, attorney for the appellee, and brother of Judge Dave W. Ling, who issued this judgment.~~

We call the attention of this Appellate Court to that part of the record on pages 379 and 380 which we quote:

“Q. (by Mr. Wilmer). Going back just a minute, Doctor, on the geology of this situation. Generally speaking, can you tell whether the mountain range which lies to the, I believe you said to the—maybe you better say. Have you prepared a diagram?

A. I have prepared a rough sketch showing the trend of the mountain range from the Big—from the Aquarius Mountains, the Grayback Mountains, the Miller Mountains, and Big Ship Mountains. It is the mountain range extending from north northeast to south southwest.

Mr. Wilmer. May I have this marked for identification?

The Clerk. Defendant's Exhibit Q for identification.

(Said document was marked Defendant's Exhibit Q for identification.)

Mr. Wilmer. So the court and counsel can see what you are doing, Doctor, I will put this on the Board.

Q. (by Mr. Wilmer). Now, Doctor, would you explain the diagram you have prepared, and identified first all the various (42) points?

Mr. Morgan. We object to that unless it has been offered in evidence.

The Court. We can use it until Mr. Fletcher testifies. Go ahead." (R. 379-380.)

Mr. Fletcher never had appeared before this Court on this case.

The Court in effect made a ruling which is based on knowing beforehand what a witness not before the Court will testify and what the effect of the testimony of this witness will be.

This case has been before the Court for ten years. Appellee knew in 1949 from the report of the engineer (14248, R. 119) of the Water Commissioner that it was drying the creek and therefore it was taking the water of the appellant.

The principle on which appellee prosecutes this case is that justice delayed is justice denied.

Case 321 was brought to delay justice in this present case and it should have been dismissed as a collateral attack as the Circuit Court remarked in the oral argument of that case. The present judgment being openly and clearly contrary to the law and contrary to the settled laws of logic it appears to have the same effect, that is, a delay of justice, as counsel for appellee must have known that reversal of this judgment was inevitable.

It took three years for the District Court to exercise its jurisdiction after case 221 was submitted, from June 1954 to April 17, 1957 (R. 646-647).

In view of the disposition the District Court made denying injunction appellants believe that they were entitled to an earlier decision so they could appeal their case.

~~Appellants therefore respectfully submit and petition this Appellate Court that if the present case is reversed, as appellants believe it will be, to instruct the District Court of Arizona to secure the services of another judge to enter judgment and determine the damages for appellants.~~

Regarding the above request it should be noticed from the Record that appellants changed eight attorneys during this litigation (R 638-649).

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### THE LAW OF THE CASE.

Appellee attempts to represent to this Court that the issues decided in cause 321 were such that the Rule of Law case is inapplicable in the present case 221.

The contradiction of its assertion becomes apparent from its own writings.

Appellee states (App. Brief page 27):

“That the Court collaterally made a finding to the effect that the main cause of appellant’s non-user was use by Bagdad.”

On page 46 of Bagdad’s brief in cause 321 we find Bagdad representing this Court that “Any rights defendants ever had were forfeited through non-user”.

It is apparent that if the main issue made by Bagdad in cause 321 was that Zannaras-Robinson lost their right

through non-user and the Court found as they state above that the main cause of Zannaras-Robinson non-user was use by Bagdad. Then the issue of the deprivation of the Zannaras-Robinson water was necessary for the just disposition of Cause 321 and became the law of the case by the affirmance of said cause.

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### **PRIMA FACIE CASE.**

Appellee in its brief (page 31) states the failure of the water to reach the Zannaras point of diversion was directly related to the soil conditions and topography and not to the relatively small amount of water pumped by Bagdad.

That this statement is incorrect is affirmatively shown by the Federal Government water gauge readings shown in appendix A of our opening brief according to these gauges.

The total water left by Bagdad to pass its point of diversion from May 1, 1949, to May 1, 1951, was 4343.3 acre feet in two years, or 2186.6 acre feet per year. Bagdad takes out 1100. acre (R 471) feet or it removes according to the gauges the one third of the yearly flow of the creek, and for five months in the summer and fall it leaves practically nothing in the creek.

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### **CHANGE OF METHOD AND MEANS OF DIVERSION.**

Bagdad admits the changes it made but insists that this change is a water salvage operation. It saves water, and

it is entitled to it, and to support the incorrect assumption that it saves water where in fact it takes water belonging to the appellants, and wastes water by evaporation, cites numerous cases in its brief on page 32 applicable in salvaging water, but inapplicable in the present case because this is not salvage operation.

The results of this so-called salvage operation were:

(1) Building a dam illegally by moving two million yards of earth (R 172-175).

(2) Impounding and storing illegally 325,000,000 gallons of water (R 585-587).

(3) Created a 100 acre lake (R 586).

(4) It caused a loss by evaporation of 200,000,000 gallons of water, which condition was not existing before the changes were made (R 560).

(5) It dried up the creek at Zannaras-Robinson diversion point for five months each year, as found in cause 321 affirmed by this Appellate Court (229 F. 2d 920) (14248 R 39).

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**“ADMITTED USE MORE WATER THAN ENTITLED TO USE  
UNDER CERTIFICATE OF WATER RIGHT.”**

**“USE OF WATER FOR PURPOSES OTHER THAN  
ITS OWN MINING OPERATION.”**

Appellee attempts to represent that the figure showing that 1100 acre feet are pumped out of the creek by Bagdad is based on assumptions.

The record affirmatively shows that this figure is reached by meter readings. Mr. Thiele testifying stated:

“Q. And the Bagdad discharge or take out from the river is computed on what basis?

A. On the measuring value—on the meter reading values.

Q. In other words the amount, the figures that you have on Bagdad are related to the actual water taken out.

A. Yes.” (R 471).

The record shows that none of the companies receiving water from Bagdad are related to it; neither does it support appellee’s statement that the amount of water involved is inconsequential and appellee must be enjoined.

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#### **FINDINGS OF THE STATE ENGINEER.**

The casual testimony of a witness, quoted in appellee’s reply brief is shown by the record to be the Engineer of the Water Division who has custody of the original records of the Water Commissioner of the State of Arizona (R 322). His testimony is from an official report (14248 R 111), which report, as the record shows, was received in time by Bagdad (14248 R 119).

Bagdad was informed officially by the Water Commissioner of the State the conditions it was creating in 1949 at Zannaras-Robinson point of diversion by drying up the creek, yet up to 1951 the entry of the judgment of the 1949 trial was representing to the District Court that there was plenty of water for Zannaras-Robinson and then it reversed its position with a new theory.



There is no attack whatsoever as to the facts testified by the Engineer of the Water Commissioner of the State of Arizona that the creek was dry in November.

Appellee is equally silent on the testimony of Mr. Sherman O. Decker, Engineer in charge of the U. S. Geologic Survey Surface Water Division, who testified (14248 R 128-130) that the creek was dry on November 23, 1950, and identified the Zannaras-Robinson photographs.

The testimony of the above engineers is unimpeachable as to impartiality, competence and authority. It is in sharp conflict with the findings of Court that from September there is water for both parties.

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#### **TESTIMONY CONTRARY TO THE WEIGHT OF THE EVIDENCE.**

Appellee failed to give any answer on the following questions raised in appellants' brief which clearly supports that the judgment is contrary to the weight of the evidence.

(1) The testimony of Mr. Sherman O. Decker, Engineer of the U. S. Geologic Survey Surface Water Division, showing that the creek was dry on November 23, 1950, while the Court's finding is that from September there is sufficient water for both parties.

(2) The testimony of Mr. C. H. W. Smith, Engineer of the Water Commissioner of the State of Arizona, testifying to the same effect as Mr. Decker above.

(3) It failed to answer about appellee's sworn testimony that in 1939 at a time prior Zannaras-Robinson or

Bagdad were taking any water from Burro Creek there was a minimum flow of 1000 gallons per minute even in the dry seasons.

(4) *It completely failed to answer or give any comment whatsoever on the most important exhibit in this case, the Federal Water Gauge reading showing the water appellee leaves in the stream for Zannaras-Robinson use.*

(5) It failed to answer about the interference with the underflow of the creek.

(6) It failed to answer with the interference of the natural bed of the creek.

(7) It failed to answer for the illegal storage of 315,000,000 gallons of water.

The failure of appellee to answer these questions must now be assumed as admitted.

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### **WATER RIGHT A PROPERTY RIGHT.**

Appellee states in its brief (page 36):

“Certainly, too, it is significant that appellants have made no effort to tap the water moving in the gravels at their point of diversion . . .”

The appellee definitely and repeatedly represents to this Appellate Court that appellants must dig and keep on digging in the bed of the creek until they get water. The record shows that appellee made such an effort by making a deep pit (Exhibits 4-16) at their point of diversion without success.

Mr. Charles Everett Trygg, Sanitary Engineer for the State of Arizona, an impartial witness, testified in the 1952 trial as follows:

“Q. I will ask you to look at 4-16. Do you remember what that represents?

A. I think this was an attempt by someone to get water, they dug a large pit, it was pretty dry when I was up there.

Q. Was that up at the Bagdad sump?

A. It was comparatively close to it. Yes.” (14248 R 134).

Zannaras-Robinson pled in their amended petition for relief as follows:

*“That plaintiffs are entitled to the flow of the stream in the manner and form in which it was before defendant’s acts reduced the flow of the stream as above stated dried up the flow entirely”* (R 20).

That the appellants are entitled to have the creek flow as it was flowing at the time of the initiation of their water right is supported by ample authority as quoted below:

In *Comstock et al. v. Ramsay*, 133 P. 1107:

“The Court said to the proposition that appropriations of water out of a natural stream for irrigation purposes, with priorities decreed, are entitled to have the conditions substantially maintained upon the stream as they were when the appropriations were made and have existed during the continuance and perfection of such appropriations. We cite the following authorities:

Handy Ditch Co. v. Louden Irrigating Canal Co., 27 Colo. 515, 62 Pac. 847; Ft. Lyon Canal Co. v. Chew, 33 Colo. 392, 81 Pac. 37; New Cache La Poudre Irri-

gation Co. v. Water Supply & Storage Co., 29 Colo. 469, 68 Pac. 781; Baer Bros. Land & Cattle Co. v. Wilson, 38 Colo. 101, 88 Pac. 265; Cache La Poudre Reservoir Co. v. Water Supply & Storage Co. et al., 25 Colo. 161, 53 Pac. 331, 46 L.R.A. 175, 71 Am.St. Rep. 131; and Voget et al. v. Minnesota Canal & Reservoir Co. et al., 47 Colo. 534, 107 Pac. 1108.”

In the present case the water rights of the parties are decreed and affirmed by the Appellate Court according to the terms of said water rights.

Appellants’ water right was perfected on January 2, 1945 (14248 R 23). Appellee’s water right was perfected on April 12, 1944 (14248 R 399). Appellants are using the water for 18 years from natural flow of the creek. Appellants have the right to insist that the conditions be maintained upon the stream as they were when their appropriation arose.

Appellants cannot be required now to dig into the gravel of the creek for water as Bagdad now proposes to this Appellate Court they should do.

As to the right of Zannaras-Robinson to the natural flow of the creek we quote from a decision of this Appellate Court in *Rickey Land & Cattle Co. v. Miller & Lux*, Circuit Court of Appeals, Ninth Circuit, March 4, 1907, 152 Fed. 11.

“The right of an appropriator of the water of stream, for the purpose of irrigation, to have the water flow in the river to the head of its ditch is an incorporeal hereditament appurtenant to the ditch and co-extensive with the owner’s right to the ditch itself.”

District Judge Wolverton says:

So also in *Wyatt v. Lorimer & Weld. Irr. Co.*, 33 Pac. 144, 18 Colo. 298, 36 Am.St.Rep. 280, Mr. Justice Coddard speaking for the Court says:

“That a valid appropriation of water from a natural stream constitutes an easement in the stream and that such easement is an incorporeal hereditament the appropriation being in perpetuity, cannot well be disputed.”

And after citing Washburn on Easements and Servitudes and Angel on Water Courses proceeds:

“The right acquired to water by an appropriator under our system is of the same character as that defined by the foregoing authorities as an incorporeal hereditament and easement. The consumer under a ditch possesses a like property. He is an appropriator from the natural stream, through the intermediate agency of the ditch, and has the right to have the quantity of water so appropriated flow in the natural stream and through the ditch for his use.”

And generally, it is held:

*“The right of the prior appropriator to have the water flow in the stream to the head of his ditch is an incorporeal hereditament appurtenant to his ditch and coextensive with his right to the ditch itself.”*

*Willey v. Decker*, 73 Pac. 210, 225, 11 Wyo. 496, 100 Am.St.Rep. 939; *Smith v. Denniff*, 60 Pac. 398, 24 Mont. 20, 81 Am.St.Rep. 408.

Or putting it in another form that:

“A right to divert and use the waters of a stream, acquired by appropriation is a hereditament appur-

tenant to the land for the benefit of which the appropriation is made.”

*Conant v. Deep Creek & Curlew Val. Irr. Co.*, 66

Pac. 188, 23 Utah 627, 90 Am.St.Rep. 721.

The principle of the right of an appropriator to the natural flow of the creek is discussed in Kinney on Irrigation & Water Right, Vol. 3, 2nd Ed., pp. 1610, 2931.

Under an appropriator's right to an injunction for unlawful diversion or diminution of quantity.

“A person who has acquired the right to the use of a certain quantity of water by an appropriation of the same or one who has in some lawful manner succeeded to the rights of an appropriator, is entitled to have the water continue to flow in the natural stream, or after diversion in his ditch, canal or other works so that he may continue to enjoy its use. Such right is a property right of which the owner cannot be deprived without due process of law and upon the payment of just compensation.

“Therefore, for the protection of such property right, and against the wrong-doer unlawfully diminishing the quantity of water to which the prior appropriator is entitled, by the unlawful diversion of the same, or otherwise, equity affords the appropriate remedy by way of an injunction. This is no modern Rule of Law, but has been enforced ever since the earliest times when the arid region Doctrine of Appropriation was adopted in the Western States of this country.”

Appellee states in its brief (page 21) there is no provision in the certificate of water right that appellants are entitled to this relatively small amount of water

pro rata per day, per week, or per month (Plfs. Ex. A in Evid. 14248 R 22).

Appellants' certificate of water right (14248 R 22) specifically states that such water right was made under application No. A-2362 Permit No. A-1539 and also made proof to the satisfaction of State Land Commissioner of Arizona. That is proof of appropriation.

Application No. 2362, Permit No. 1539 (14248 R 13-17) and proof of appropriation (14248 R 18-22) were pled by Zannaras-Robinson in civil cause 321 consolidated for trial with cause 221 Prescott by attaching the said documents to the pleadings and made part thereof as Exhibit A (14248 R 13-24).

These documents are inseparable parts of the water right and expressly declare the conditions and detailed terms of water right No. 1341 granted to Zannaras-Robinson by the State of Arizona.

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#### **TERMS OF ZANNARAS-ROBINSON WATER RIGHTS.**

- 1) *Amount* not to exceed 3,000,000 gallons annually (14248 R 14)
- 2) *Priority*—August 27, 1940 (14248 R 22)
- 3) *Source*—Burro Creek (14248 R 13)
- 4) *Time for use of water*—The year around (14248 R 18)
- 5) *Diversion*—Directly from the flow of creek, no dam (14248 R 14)

- 6) *Rate of removing* water from creek 60 gallons per minute (14248 R 19)
- 7) *Means of Diversion*—By pumps, engine, pipe, etc. (14248 R 14)
- 8) *Purpose of Use*—Mining and Domestic (14248 R 18)

The Zannaras-Robinson water rights were adjudicated and affirmed and specifically stated that such adjudication is made according to the terms of said water rights in the judgment of cause 321 consolidated for trial with 221 (14248 R 42).

Zannaras-Robinson according to the adjudicated terms of their water right are entitled to pump water out of the natural flow of the creek the year around at the rate of 60 gallons per minute, and by the means of diversion as indicated in the water right certificate.

It therefore appears that appellee's statement that there are no provisions in Zannaras-Robinson water right as to time and rate of water to be taken out are incorrect.

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#### **SUMMARY OF APPELLEE'S ARGUMENTS IN ITS REPLY BRIEF AND APPELLANTS' ANSWERS.**

APPELLEE STATES:

- 1) That it built a dam to salvage water and that it is entitled to this water.

- 2) That its use of water does not interfere with appellants' water ascertained by expert opinion that water would not reach appellants' diversion point as it will be wasted by evaporation.



- 3) Appellants should dig in the gravel for water.
- 4) Appellants should have taken notice of creek conditions at the time of the initiation of their rights (R 35-36).
- 5) Last judgment of the District Court (April 17, 1957) denying injunction to Zannaras-Robinson controls.
- 6) Res judicata not brought to the attention of the Court.
- 7) Judgment of 1951 not reviewable.

#### APPELLANTS ANSWER:

1 and 2) Salvage operation, actually illegal diversion and extended use taking appellants' water, creating waste by evaporation.

3) Appellants insist that the natural flow of the creek is part of their adjudicated right and property. They cannot be compelled to dig in the creek for water.

4) Appellants insist that appellee should have taken notice of the creek conditions at the initiation of appellee's water rights as a junior appropriator. *State ex rel. Crowley v. District Court of Sixth Judicial Dist.*, 88 P. 2d 23.

5) Appellants insist that deprivation of their water by Bagdad has been decided in case 321 consolidated for trial with case 221, the present case. After affirmance of 321 appellants invoked the Law of the Case. Appellants claim the District Court's judgment is void as being contrary to the mandate and also based on the proceedings of 1954 when the District Court had lost jurisdiction.

6) Res judicata pled distinctly before the District Court.

7) Appellants insist that the Judgment of 1951 is reviewable, and seeks according to the pleadings the following (R 3-7; R 18-21):

a) Mandatory injunction to compel appellee to let the water down for restoration of appellants' property to the condition it was before being disturbed and wrongfully changed by appellee.

b) Prohibitive and perpetual injunction from illegally diverting and storing the water of Burro Creek, Boulder Creek and their tributaries.

c) Prohibitive and perpetual injunction from interfering with the natural flow of Burro Creek, Boulder Creek and their tributaries, to which the appellants are entitled.

d) Prohibitive and perpetual injunction from interfering with the bed and underflow of Burro Creek, Boulder Creek and their tributaries.

e) Prohibitive and perpetual injunction not to divert more water than appellee water right calls for and not to divert water for other uses than for the purpose of its water right by giving water to other mining operations.

f) That the Court determine appellants' damages according to their pleadings from June 28, 1948, until such time as appellee ceases its interference with appellants' water right, together with costs.

**CONCLUSION.**

It is the belief of the appellants that appellee failed to overcome appellants' affirmative proofs of the reasons for which the judgment of the District Court should be reversed, and respectfully submits that judgment be reversed with directions to enter judgment for Zannaras-Robinson as prayed, in accordance with instructions of this Appellate Court.

Dated, March 14, 1958.

Respectfully submitted,

JOHN PHILLIP ZANNARAS,

J. P. ROBINSON, JR.,

U. S. TUNGSTEN CORPORATION,

*Appellants.*



**No. 15640**

IN THE

**United States Court of Appeals**

**For the Ninth Circuit**

**1957 TERM**

JOHN PHILLIP ZANNARAS,  
J. P. ROBINSON, JR. *and*  
U. S. TUNGSTEN CORPORA-  
TION,

*Appellants,*

*vs.*

BAGDAD COPPER CORPORA-  
TION, a Corporation,

*Appellee.*

*Appeal from the United  
States District Court for  
the District of Arizona*

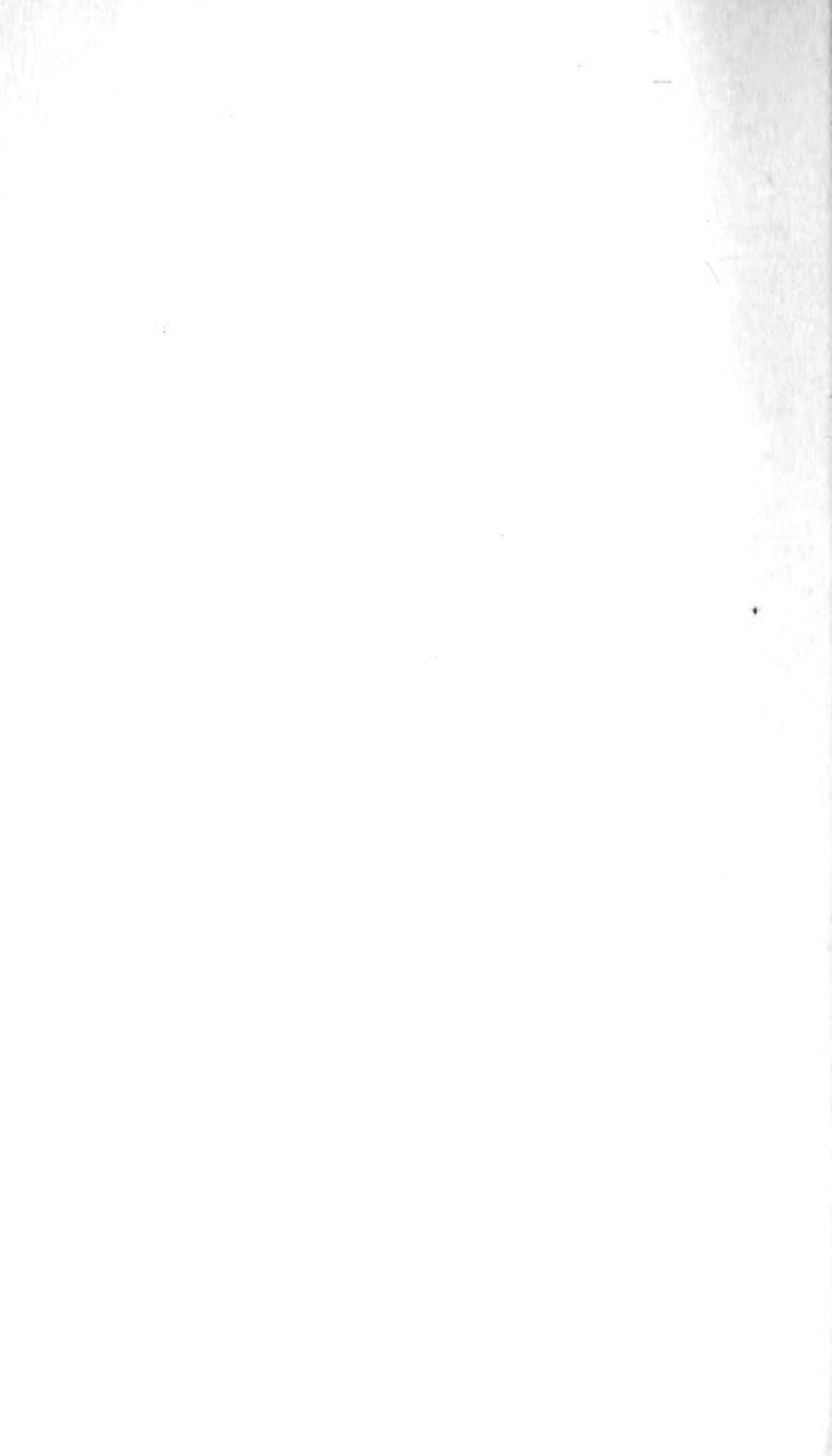
**BRIEF OF APPELLEE**

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**FILED**

FEB 25 1958



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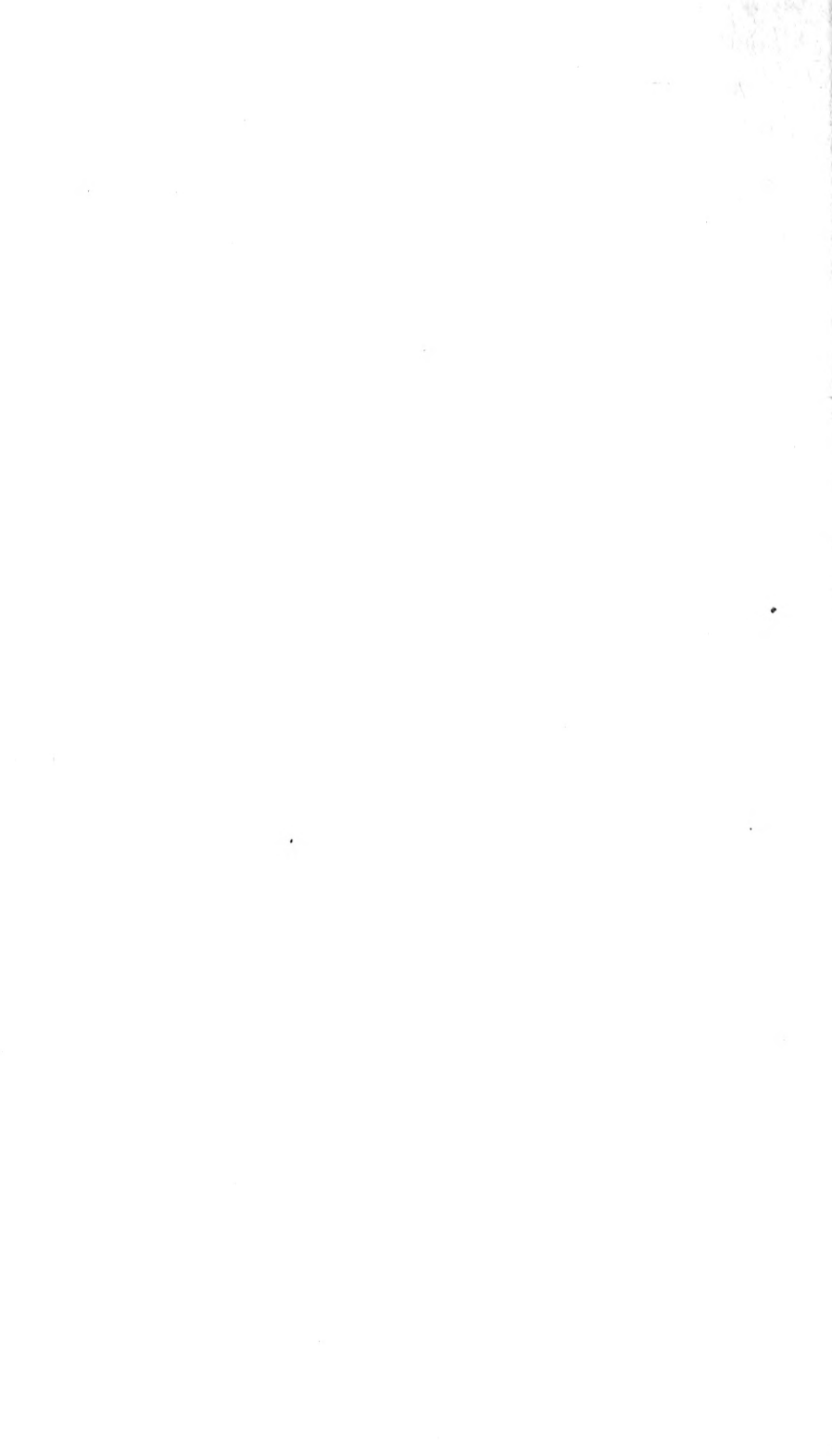


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IN THE

**United States Court of Appeals**

For the Ninth Circuit

1957 TERM

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JOHN PHILLIP ZANNARAS,  
J. P. ROBINSON, JR. and  
U. S. TUNGSTEN CORPORA-  
TION,

*Appellants,*

*vs.*

BAGDAD COPPER CORPORA-  
TION, a Corporation,

*Appellee.*

No. 15640

*Appeal from the United  
States District Court for  
the District of Arizona*

**BRIEF OF APPELLEE**

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**PREFACE**

Appellants have so thoroughly commingled the relevant with the irrelevant that a Motion to Strike from the Record and their Opening Brief would but add to the confusion. In effect, appellants, despite the fact that there was no order of consolidation (14248 R. 52, 53, 54, 27, 28, 29, 30, 31, 32) have incorporated the testimony and evidence taken in another cause, No. 321, affirmed in this Court (229 F. 2d 920) into their statement of the case. In addition, they have gone back and indiscriminately

helped themselves to such portions of Cause No. 129, disposed of in the District Court in 1945 and of the evidence admitted on the first trial of this action in 1949 resulting in a judgment adverse to appellants from which no appeal was taken and which has long reposed undisturbed as a final judgment, as suits their fancy.

In so doing, appellants have presented an untrue and distorted picture which, if left unchallenged, cannot but leave the disturbing fear in our hearts that this Court might, perhaps unconsciously, be disturbed thereby.

Rather, therefore, than either ignoring matters not properly before the Court or requesting the Court to strike all such irrelevant matter, we shall briefly meet it head on, to the end that the Court may have what is at least our version and view of the true fact situation.

## REPLY TO STATEMENTS RE "JURISDICTION"

We quarrel not with the statements having a bona fide relation to jurisdiction. We do object to additional unrelated argument.

The judgment entered on the first trial of this action in 1949 was that "plaintiffs (appellants) take nothing by their action, and that defendant (appellee) have and recover its costs in this behalf expended or incurred." (R. 12) The Court then ordered "that this cause be retained by the Court for further orders should the same be deemed necessary *in the future . . .*" (emphasis added)

As heretofore indicated, there was no consolidation of this cause with Cause No. 321. Neither did the District Court nor this Court on appeal in Cause No. 321 "determine the same water rights" as are involved here. The sole object of Cause No. 321 as presented by Bagdad was to secure an adjudication that appellants had obtained their certificate of water right by fraud or had forfeited it by non-user. This Court agreed with the District Court that we were too late in raising the fraud issue and hence barred by limitations and that there was sufficient evidence of inter-

mittent user by appellants to defeat a forfeiture. So any statement that the purpose of this appeal is to enforce the mandate of this Court issued on the appeal in Cause No. 321 is so much nonsense.

We are sure appellants inadvertently make the assertion (p. 4) that the judgment entered by the trial court and from which this appeal is taken was after a trial "involving . . . the same water rights *and the same evidence* . . ." as Cause No. 321. Practically the entire second volume of the Transcript of Record is made up of evidence taken long after Cause No. 321 was submitted to and decided by the District Judge.

## STATEMENT OF THE CASE

### THE LITIGATION HISTORY

The trial of this cause, on its setting for further taking of testimony, was the fourth round in the legal fisticuffs quickly beginning after Mr. Zannaras arrived in the area.

#### *Round One.*

In 1944 Zannaras served notice on Bagdad that its tailings were polluting the waters of Burro Creek, to his great damage. This despite the fact a sandy, rocky stretch of Burro Creek some seven miles in length lies between. Suit was filed for an injunction and \$35,000 general and exemplary damages. The present management had just taken over and it proceeded promptly to rearrange its tailings disposal method by constructing a dam across a canyon whereby the tailings were impounded, thereby making further claim of pollution impossible and also enabling Bagdad to reuse the water after the tailings had settled out. (14248 R. 292)

On February 14, 1945 (14248 R. 370) Bagdad's general manager advised Zannaras by letter that the conditions which permitted tailings to escape had been corrected and that the creek water was clear. On February 16, 1945, Zannaras filed his damage suit, Cause No. 129, United States District Court, Prescott, despite the fact Bagdad had corrected the condition within the

sixty day period proposed by Zannaras in his letter of December 16, 1944. (14248 R. 369)

After a day's trial, since the condition could not now re-occur, to avoid the expense of a long trial, Bagdad agreed to an injunction and to what was, in practical effect, a judgment for nominal damages with each party to pay its own costs. (14248 R. 395, 396)

An interesting sidelight on this marathon litigation is afforded by this admission by Mr. Zannaras testifying on the trial of this action in July, 1945 (14248 R. 395):

"Q. Did you at that time say to Mr. Greene and to Mr. Dickie (Bagdad management) that your price was \$75,000.00 and any time that they had to have it it was neither more nor less? Did you make that statement?

"A. Not in that form."

### *Round Two.*

July 12, 1948 Zannaras filed suit in the United States District Court against Bagdad, Cause No. 221, seeking damages and an injunction, alleging that Bagdad was usurping the water which otherwise would service the appropriation of Zannaras. Issue was joined and the cause was tried before the Court without a jury beginning March 3, 1949. Extensive testimony was taken not only upon the issue of the availability of water to Zannaras but also as to whether in fact *Zannaras had any bona fide use for the water claimed.*

The Court made a Finding of Fact in denying Zannaras relief:

"That plaintiffs have failed to prove by a preponderance of the evidence that plaintiff suffered any loss of profits by reason of any improper diversion of water by defendant, or that said plaintiffs have been interfered with *in the operation of or carrying out of any bona fide mining or milling activity* by any wrongful diversion of water by defendant, Bagdad Copper Corporation." (No. 15640 R. 11) (Emphasis added)

The evidence to support this conclusion was ample.

The mill of appellants was ready for use in 1941. Apparently some old tailings were run through the mill in that year, although in all of his previous sworn testimony Zannaras had said his first milling operation was in the fall of 1942. (14248 R. 313, 314, 315) Apparently there was no recovery and no claim can be made by appellants that this was a beneficial use. (14248 R. 314)

In 1942, although there was ample gold ore available:

"Q. How do you know you had plenty of ore?

"A. I could see the Mystery Mines in the locality up there, rich bars of gold ore.

"Q. At the Mystery Mine?

"A. Not only at the Mystery, in all that vicinity." (R. 109) only a few tons of ore were milled, probably in the neighborhood of 10 tons. (14248 R. 315, 316, 317) None of the resulting concentrates were sold. (14248 R. 317); they were just left at the mill. (14248 R. 325) In December of 1943 appellants shipped 10 tons of raw ore to the Phoenix stockpile, receiving a net return of \$358.34 (14248 R. 373) In that month they claim they started to mill — milled 7 - 10 tons, and that thereafter the water was bad so they suspended operations to November of 1944. (14248 R. 375, 385) In November of 1944 again the standard 7-10 tons were milled. (14248 R. 385) These concentrates apparently were also just left at the mill. (14248 R. 389) Appellants admit that by May of 1945 the water was entirely cleared up. (14248 R. 408) The mill was probably operated once in 1945, with about 6 tons of ore milled. (14248 R. 408) Thereafter, except for some claimed "trial tests" (14248 R. 336), "checking the condition of the mill," no attempt was made to operate the mill until June of 1948 when, appellants claim, there was no water available. (14248 R. 342)

Robinson went into the Army in the summer of 1945 and returned from service in the summer of 1947. (14248 R. 336, 339) His only experience as a miner prior to coming to Arizona in 1940 was in working as a coal miner in Pennsylvania (14248

R. 306); yet Zannaras testified that he shut down to await the return of Robinson from the Army (14248 R. 337) because he couldn't hire any qualified labor to replace him. (14248 R. 336) After the return of Robinson from the Army in 1947 the explanation for failure to operate is touching:

"Q. Why didn't you go ahead and put your mill back in operation then?

"A. Because Mr. Robinson wanted to be near his wife. He brought his wife from the other side and he wrote me a letter he wants to stay near his wife, for a few months until she got used to the desert, so we decided to build a laboratory.

"Q. Was there anything to keep Mr. Robinson from staying at the mill and being near his wife, and you directing the operations of the mine? I mean there wasn't any need for Mr. Robinson, you could hire plenty of men?

"A. I will tell you, a man and a wife and a girl coming from the other side and they are on the desert in Arizona is something different. I don't know whether you realize it or not. Mr. Robinson wanted to be near his wife and I justified him 100 per cent, I—Remember I make sacrifice to him to go ahead and built the laboratory, something we needed there.

"Q. Your mine was about, say eight miles away from your mill?

"A. About ten miles.

"Q. Was there any reason why you were afraid to go to the mine without Mr. Robinson being with you?

"A. Went to the mine?" (14248 R. 340)

The Court had in addition as a backdrop against which to judge the sincerity and truthfulness of Zannaras' testimony as to his bona fide intentions, his testimony, solemnly given under oath, that, in putting 3,000,000 gallons of water per year to beneficial use not to exceed five men drank, used for bathing, cooking and cleaning the house 2,000 gallons of water every day, used 1,000 gallons every day except Sundays in washing the floor of



the mill and, for operating a jackhammer and wetting down ore, 8,000 to 10,000 gallons per day. (14248 R. 413 - 422)

*Rounds Three and Four.*

In this Cause No. 221, pursuant to reserved jurisdiction, appellants filed a "Petition for Relief" on February 8, 1951 which was amended March 28, 1951, claiming again that Bagdad was usurping appellants' water. Issue was joined and the matter set for hearing.

On March 5, 1951, Bagdad filed Cause No. 321 in the District Court praying cancellation of appellants' water right for fraud in its procurement and in the alternative cancellation for non-user resulting in statutory forfeiture. Issue was also joined in this cause and it was set for hearing on the same day as the further hearing in Cause No. 221.

On May 13, 1952, the Court proceeded to first hear the evidence in Cause No. 221 (14248 R. 26, 28, 51, 52, 53) and then to hear the testimony in Cause No. 321 (14248 R. 141) which also constituted Bagdad's rebuttal and both causes were submitted on briefs. (14248 R. 32, 367, 368) On July 6, 1953, the Court, by minute order (14248 R. 32) found the issues for defendants in Cause No. 321. Findings of Fact and Conclusions of Law were settled and judgment rendered for defendants, which on appeal this Court affirmed.

*On the same day* that by minute order in Cause No. 321, the Court found the issues for defendants (appellants) in Cause No. 221, the Court vacated its order of submission *for the purpose of taking further evidence* (R. 644) and the matter was finally set for taking additional evidence on March 9, 1954. On this hearing, which lasted three days, appellee, Bagdad, presented a large amount of scientific and engineering evidence, after which the matter was again submitted.

### STATEMENT OF THE CASE

In 1941 appellants had their mill completed (so they claim) and ready for use; they had a large ore body of high grade gold ore

blocked out and ready to mine and mill. (14248 R. 312, 313) But Zannaras only milled (so he says) some tailings, operating only 6 - 8 hours in 1941. (14248 R. 313)

So now, appellants being all set up and ready to mill gold ore, turned from the gold property to tungsten. A total of 8 - 10 tons of ore was milled in 1942 but no effort was made to commercially dispose of the end product. (14248 R. 316, 317, 325)

Then appellants moved to another part of their claims (14248 R. 317) and in 1943 either the mill was not operated at all or only briefly in November or December "for operating purposes." (14248 R. 325, 326) The total ore milled to December of 1944 from the start of the enterprise was 8 - 10 tons.

"Q. Well now, how much ore had you put through your mill prior to the 1944 operation?

"A. 10 or 12 tons — 1944?

"Q. I mean between the time you milled the 10 or 12 tons and the time you shut down in December 1943, how much did you put through?

"A. I don't get the question.

"Q. Between the time when you milled the 10 or 12 tons until the time you shut down in December of 1943?

"A. No, I didn't mill any during that time.

"Q. In other words, up to the time you shut down in December 1943, you had put 10 or 12 tons through the mill?

"A. That is right.

"Q. Then in the latter part of 1944 you ran the mill for a day?

"A. Yes.

"Q. Can you tell us approximately how much ore you put through it?

"A. About 10 tons.

"Q. And what was done with those concentrates?

"A. I have them." (14248 R. 328, 329)

Appellants excuse non-operation through 1944 on the basis that the finely ground tailings of Bagdad, after traveling seven miles through a sandy stream bed, so polluted the water it wore out his pump and was unusable. (14248 R. 330, 331)

From and after May, 1945 the water was clear and plentiful (14248 R. 331) but other than for a few claimed "test runs" no effort was made to operate through 1945, 1946 or 1947. This non-operation was substantially without excuse. (14248 R. 335, 336, 337, 338, 339, 340, 341, 342)

Failure to operate in 1948, by the judgment of the Court in Cause No. 221 in favor of Bagdad cannot be charged to Bagdad since the judgment found that Bagdad had not deprived appellants of water during that year.

In 1949 appellants claimed to have milled tungsten ore variously described as "several truck loads," (14248 R. 343) "probably over a hundred tons," (14248 R. 344) "approximately a hundred tons." (14248 R. 344)

In 1950 appellants claim to have milled 200 to 300 tons of gold ore (14248 R. 344, 345) but for some reason the resulting concentrates were not sold but left at the mill. (14248 R. 96)

For some reason, when there was ample water, appellants either worked the ore bodies or rebuilt or overhauled the mill, and it was only in seasons of expected shortage of water they tried to mill.

"Q. Why didn't you have your mill overhauled and ready to go when the water came?

"A. I started already. I bought machinery and improved my mill. I installed a classifier.

"Q. Why did you have to wait until the water came before you started putting your mill in shape to run?

"A. Now let me get the question. You want me to start working and get ready for the water. We were doing work around here. Now I remember we were working the gold

claim. I had an employee by the name of Warren Lyman. We were working the gold claim.

"Q. From November 17 on what did you do with respect to running your mill?

"A. Running the mill? I told you I started to overhauled the mill and installed a classifier.

"Q. That is after the water was rolling by.

"A. Yes.

"Q. Why hadn't you done it before?

"A. We were developing ore.

"Q. Now isn't it a fact, Mr. Zannaras, every time the water started you found some excuse not to start your mill up until just recently.

"A. Any time I started it takes me about 1½ months to overhaul the machinery." (14248 R. 97 - 98)

Subsequent to the trial in 1952, Bagdad began an investigation of the possibility of building a dam to store flood waters, thereby stabilizing the flow of the stream and solving the summer water shortage (R. 611, 612) and applied for a permit for a dam site from the State of Arizona. Zannaras, despite the fact his diversion is for only 3,000,000 gallons per year (10 acre feet total) and the fact that a reservoir impounding 20,000 acre feet of flood water which now is wasted would solve everyone's problems, not only protested Bagdad's dam permit application, but filed an application for a reservoir right-of-way which paralleled the site as disclosed by Bagdad's engineering data filed with the State Water Commissioner and Bagdad moved its dam site down creek one and one-half miles. (R. 611, 612, 596, 597) Probably the closing testimony by Zannaras at the 1954 hearing best summarizes the situation:

"Q. Do you have any records of how much money you have actually realized from any milling operations there?

"A. Yes.

"Q. Do you have any records?

"A. Yes, we have records.

"Q. Where are they?

"A. Up at the place, in the mines.

"Q. What do they consist of?

"A. The returns. They sent us a return.

"Q. Do you have an actual book which shows the amount of concentrate sold and the price for it?

"A. We may have the returns.

"Q. Do you have a record to keep track of what you get from selling concentrates?

"A. I may have.

"Q. Don't you know?

"A. Because we were reorganizing at the time. We were reorganizing the company.

"Q. What did you use for making out income tax returns?

"A. We have got records.

"Q. You have got records which show just what you are taking in from your operations?

"A. It was just testing operations, don't forget that. It is just testing.

"Q. You were testing since 1942? That is in substance what you have been doing up there, testing and developing new mines?

"A. We were developing the mine, and I built a big mill up there now, and it takes time.

"Q. Your mill at Burro Creek has been ready to run since 1942, has it not?

"A. Ready to run?

"Q. Yes, been ready to operate since 1942?

"A. I told you we developed the mine. The mill was ready to receive ores.

"Q. Since 1942 the mill at Burro Creek, according to your testimony, has been in a condition to operate, has it not?

"A. Yes, it will operate.

"Q. Since that time you have continued to revise the mill and open new mining bodies, but have done no mining, substantially?

"A. Well, substantially, there is nothing."  
(R. 605, 606)

In the light of the foregoing it is rather apparent that the huffing and puffing which appellants resort to in the Opening of their Statement of the Case to the effect they had a five year contract with the U.S.G.S.A. for their production of tungsten is so much hot air. The facts are, by Zannaras' own admission, that up to March of 1954 the contribution of appellants to the economy of the state or nation by way of production of tungsten or any other mineral of value was in practical appraisal exactly nil and, insofar as custom milling ore for others is concerned, the two victims of this "commercial" activity testified in the 1952 hearings. Alvis M. Short testified he took 7 tons to the Zannaras mill in 1950 from which 100 pounds of concentrates were obtained which did not meet government specifications but had to be recleaned yielding thereby 60 pounds which he sold for a total of \$58.00. The milling charges were \$60.00. Seven tons of similar ore milled at Kingman, Arizona, yielded 1,000 to 1,100 pounds of concentrates and brought about \$2,500. (14248 R. 237, 238)

William L. Nutter took 5 tons of crude ore and 1,500 pounds concentrates to the Zannaras mill in 1951 which should have given a recovery in the neighborhood of \$1,000. The settlement sheet from Zannaras was around \$7.00. (14248 R. 320, 321, 322) No evidence of substantial character was offered to substantiate any of the claims Zannaras made as to expenditures or otherwise.

In preparation for the 1954 hearing Bagdad employed the services of Dr. Heinrich J. Thiele and Professor Herbert C. Fletcher to make a study of the water supply, the topography, soil condi-

tions and related physical facts in the expectation of establishing some formula by which water releases at the Bagdad diversion could be fixed by the Court thereby ending the recurring harassment of claims that water due Zannaras was being denied him. These two thoroughly competent scientists arrived at some rather startling conclusions which, however, completely supported the testimony of numerous witnesses given during the 1952 hearing hereafter referred to.

Dr. Thiele, a resident of Tempe, Arizona, is a graduate of the Clausthal School of Mines in Germany, the Montana School of Mines, Butte, Montana and the Technical University of Berlin. He graduated in 1936 from Clausthal and then attended Montana School of Mines where he obtained his Master's Degree. He returned to Germany and worked as a ground water consultant, working for cities and large industries. He has a Doctor's Degree in Engineering, Master's Degree in Mineral Dressing and an Engineering Degree in Mining Engineering. (R. 371, 372) He returned to the United States after World War II in 1952 and is a Registered Civil Engineer in Arizona. He has taken out his first papers as a citizen.

Dr. Thiele has made an underground water study for the Salt River Valley Water Users' Association and was then engaged in a similar study for the Indian Service for the Indian Council at Sacaton, Arizona. He is the author of numerous scientific papers, a textbook and part of another (R. 379) and has lectured in ground water courses of the U. S. Geological Survey in Austin, Texas, University of Texas. (R. 399)

Professor Fletcher is a graduate of Forestry and Geology from Utah State Agricultural College and holds a Master's Degree in soils and sedimentation from the University of Missouri and has pursued his work for a Doctor's Degree in that Science at the University of Oklahoma. He is in charge of the water shed management research for the U. S. Forest Service stationed at Arizona State, Tempe, Arizona. He has been in actual practice since 1935, first with the Soil Conservation Service from 1935 to 1939. He

was in charge of the Division of Water and Forest Information for the Forest Service at Washington, D. C. and returned to the Southwest in 1948, since which time he has constantly conducted experiments, made studies and authored papers relating to water losses from soils. (R. 498, 499) He collaborated with Dr. Thiele in the studies reported to the Court.

In preparation for the study a U. S. Geological Survey aerial photo map of the Burro Creek area from the Bagdad diversion point to the Zannaras diversion point was obtained. This was turned over to George Colville, a Registered Civil Engineer who had large experience in surveying. By an actual field survey, using two survey parties over a week's time, the accuracy of this map as to the boundaries of the creek bed was confirmed and the elevations of the bed were established by cross sections. (R. 355, 357, 358, 495) The aerial photograph with the area of the creek bed colored yellow is Defendant's "N" in Evidence. (R. 357, 361) The point marked "A" identifies the Zannaras diversion point, the point marked "B" that of Bagdad. The actual cross section survey showing the basin of the creek bed is Defendant's "O" in Evidence. (R. 369, 370)

This map, "N" in Evidence, and the survey, "O" in Evidence, shows that the creek debouches from a rocky canyon or ravine (R. 383) at point "B" and spreads out into an alluvial plane extending generally northeast-southwest a distance of some 4 miles where it again contracts or pinches in on a narrow bed rock and lip and is exposed and the stream bed again assumes a somewhat thread-like appearance. The area of the creek bed in this valley or plane area within the exterior boundaries of the creek bed edges contains 1374 acres. (R. 361) Through this entire four mile stretch the water disappears underground and also comes to the surface at places and spreads out (R. 496) sometimes as much as 100 feet with saturated ground on each side as above the Kingman Crossing. (R. 497) Generally speaking, through this area there is no channel with banks on either side. (R. 497, 481, 482, Deft. Ex. "O" in Evid.) The point where the creek bed con-



stricts back to thread-like appearance is the point where the old Wickenburg-Kingman highway crosses the creek and is constantly referred to as the "Kingman Crossing." The area between the Kingman Crossing and the Zannaras diversion, a distance of about 3 miles, (R. 460, 461) was also surveyed and computed and the area within the boundaries of the creek for this area was found to make up 82.5 acres or a total creek bed area between the two diversion points of 1456.5 acres. (R. 326)

The creek bed from the Bagdad diversion to the Kingman Crossing is made up of gravels, clayey gravels, sands and silts (R. 362); from the Kingman Crossing to the Zannaras diversion it is made up of a sheet of gravel over bed rock. (R. 362) Burro Creek has an approximate elevation of 2400 feet which is substantially below the elevation of Bagdad. (R. 409)

The average width of the river channel below Kingman Crossing is 215 feet while above the crossing and to the Bagdad diversion it averages about 2,000 feet. (R. 437, 438) The slope or fall from Bagdad diversion to Kingman Crossing is approximately 400 feet. (R. 461) The slope or drop from Kingman Crossing to Zannaras diversion is 140 feet. (R. 466) The standing water level in the water well at Bogle Ranch, a point about one-half way between the Bagdad diversion and the Kingman Crossing, was observed by Dr. Thiele to be 150 inches higher in elevation than the elevation at Kingman Crossing. (R. 448, 449) The sands and gravels making up the river basin carry moisture to within one-half to one-quarter foot of the surface (R. 467) and the entire basin is overgrown to approximately a 50% density with phraetophyte type of vegetation such as cottonwoods, willow, catspaws and mesquite (not a true phraetophyte). (R. 512) Cottonwoods will use up to 6 acre feet of water, mesquite between 3 and 4 acre feet, and willow 6 to 7 acre feet. (R. 512) A phraetophyte is a water loving plant which to thrive must have its "feet" in free water. (R. 510, 511)

Dr. Thiele began his study February 18, 1954, which continued 18 days up to the trial date (R. 387) with about two-thirds of

the time actually spent in the field and on the ground. He had 4 to 6 people assisting him in the field. (R. 387)

Dr. Thiele, after making an aerial survey of the area consisting of three separate flights to study the formations, topography, etc. (R. 377) turned to the known data as to physical condition. (R. 378) He examined and tested cores from test drilling and checked the water level in wells. These drill cores went to bed rock from 100 to 400 feet (R. 435, 436) below the Bagdad diversion (about the Bogle Ranch as shown on "N" in Evidence). Some were 20 to 30 feet apart, others up to 300 feet. These tests together with the geophysical work done by Dr. Thiele demonstrated a cover of gravels and clay gravels to a depth of 90 feet in this basin, deeper in some places than others.

Dr. Thiele, by use of geophysical procedures, measured the depth and area of the creek basin from the Bagdad diversion to the Zannaras diversion. This is a procedure or method commonly employed by the U. S. Bureau of Mines (R. 375) and by the oil industry. (R. 376) It employs electrical impulses; electrodes with the penetration of the current related to the distance between the two electrodes indicating the resistivity which in turn is interpreted by the scientist in terms of depths and materials traversed by the electrical impulse. (R. 383, 384, 385, 386, 388) The percentage of error in determining depth to bedrock is 10% (R. 386). Thirty separate readings or movement of the electrodes were made at each station and 65 stations from Point A to B, Exhibit "N" were established.

By these means, Dr. Thiele plotted the depth to bed rock and the overlaying materials from Point A to B. His findings are graphically depicted in Defendant's "R" (apparently through oversight this exhibit was never formally received in evidence although fully testified to by Dr. Thiele). This exhibit presents a cross-section, lengthwise of Burro Creek from Points A to B (R. 390) demonstrating bed rock and overlaying gravels and alluvial material. (R. 390) It demonstrates Dr. Thiele's testimony that an old valley or river channel lies running in a gen-

erally easterly-westerly direction immediately below the Bagdad diversion which valley has filled with alluvial fill, fanglomerate-breccia, which is relatively impervious although with some water holding capacity. (R. 394) This is overlaid with gravels from Point A to Point B to a thickness varying from 40 feet to 7 feet with the thicker overlay prevailing. (R. 394, 395) At the Kingman Crossing bed rock slants to the surface and in effect creates a stone dam at that point over the lip of which the ground water rises and flows on the surface. (R. 393) The valley to bed rock at its deepest point is 1200 feet and the stream flows across it at an angle on top of the fill materials and through the sand and gravels. (R. 395, 396) This Exhibit "R" accurately reflects the findings of Dr. Thiele. (R. 394, 396)

The permeability of various types of soil material is well known and tables are available giving this information. (R. 401) The coefficient of permeability is important in determining the underground movement of water. The amount of flow is determined by computing the coefficient of permeability times the slope of the water table measured in feet per mile times the square section of the aggregate of the aquifer of the water bearing material. (R. 401, 402)

Assuming the highest permeability factor the maximum amount daily flowing underground at Bagdad diversion would be 9 acre feet of water; assuming the lowest permeability factor the amount per day moving underground would be one-tenth of an acre foot per day. (R. 404, 405) So long as there is live surface water in a stream the underground movement of water is unvaried. Floods or the *amount* of surface water flowing has no appreciable effect on the underground movement. (R. 415, 416) Gravels of the character here involved have a water holding capacity of about 23% with a free moving water capacity of 20%. According to Darcy's law, by which the movement of underground water is computed, water moves at from 60 feet to one-half mile per year depending on permeability and slope. (R. 462, 463) Hence, the water moving under the gravels would take at least two years to go from Point B to Point A.

Assuming an average of only ten feet overlay of sands and gravel in the creek bed between Kingman Crossing and Bagdad diversion this material would provide a reservoir for 2700 acre feet of water; and another 150 acre feet in the gravels between Kingman Crossing and Zannaras diversion (R. 469), one hundred fifty acre feet capacity equals about 20,000,000 gallons of free water. (R. 466)

The United States Weather Bureau has established mean monthly and annual pan evaporation rates of water at Roosevelt, elevation 2200 feet, Tucson, elevation 2423 feet, and Safford, 2900 feet, (Deft's "S" in Evid.) Annually these are, respectively, 79.87 inches, 72.71 inches, and 82.95 inches. Bagdad proper is given an annual rate of 75 inches loss (R. 405) and since it is substantially higher than the bed of Burro Creek, the Tucson figure of 82 inches is probably more accurate. (R. 417) The Bureau of Reclamation estimates the ground evaporation of the Burro Creek area at 60 inches per year. (R. 418) The figures at Roosevelt, Safford and Tucson show that June and July are the months of very high loss with an average of approximately 15% of the entire yearly loss occurring at Tucson in June with close to this in May and July.

Accordingly, as illustrative of the problem here involved, Dr. Thiele took the month of June 1953 and made a computation. First, he assumed the highest permeability of the underground at the Bagdad diversion and assumed instead of 1 acre foot a day discharge underground the maximum of 9 acre feet or 270 acre feet per month.

Next, he computed from records the entire amount of water pumped by Bagdad in June or 69 acre feet. (R. 424) He then computed from the U.S.G.S. gauge readings the amount of water passing Bagdad diversion and found a total of 295 acre feet of water in the river *above* the Bagdad diversion made up of 30 acre feet underflow, 69 acre feet pumped by Bagdad and 196 acre feet passing down the river. If we assume the maximum underflow at Bagdad diversion, or 270 acre feet instead of 30, we have a total of 535 acre feet available.

15% of the assumed evapo-transpiration of 60 inches at Burro Creek is 9 inches or  $\frac{3}{4}$ ths of 1 foot, which computed over the 1456.5 acres of creek bed gives a water loss of almost 1100 acre feet during June of that year. (R. 418, 419)

Professor Fletcher's studies chiefly resulted in two exhibits, Defendant's "Y" in Evidence and Defendant's "A" and "B" in Evidence.

The purpose of Exhibit "Y" is to graphically demonstrate the extreme rapidity with which evaporation and transpiration rate of water loss rises as the summer months come on and to relate this loss to stream and basin water supply. It also relates the long term rainfall record to this water use and demonstrates the fact that if Bagdad took no water at all in the dry summer months the most that could result to benefit Zannaras would be a delay of perhaps a week in drying up of the available water. In other words, the requirements of this large basin to satisfy the potential water loss which would follow a full supply is so great in the hot summer that the maximum draft of 94 acre feet which Bagdad can draw, if suspended, would merely afford that much more water to satisfy the evapo-transpiration potential of the basin. (R. 512, 513, 514, 515, 516, 517, 518, 519, 520, 521, 522, 523, 524, 525, 527, 528, 529, 530, 531, 532, 533, 564) None of it would reach the Zannaras diversion. He estimated the evapo-transpiration requirements of the valley in June and July at in excess of 800 acre feet input (R. 520, 521); and that in June and July the lower part of the basin would lose more water than a free water surface while the higher or upper end would lose less. (R. 563)

It was the unanimous and firm conclusion of both Dr. Thiele and Professor Fletcher that the amount of water taken by Bagdad during the months of low water supply and high water loss through evapo-transpiration did not substantially contribute to the water loss complained of by Zannaras. (R. 428, 521, 522)

There was no evidence offered to contradict or impeach the validity of their conclusions other than by reference to the fact

that on occasions through the summer water does run in the creek. This was well answered by Professor Fletcher (R. 534, 535):

"Q. Now, this figure that you have there, as to the loss in evaporation over the basin, that represents an average overall picture, is that the case?

"A. That is right. Yes, you can't just tie it down to one particular location like this. This is an average, taking the average of precipitation for that particular weather station.

"Q. For that area?

"A. For that area.

"Q. That is the reason, I take it, why you might go out there in July or August and find free running water when you theoretically wouldn't find it on the basis of a long-term investigation?

"A. Yes."

The conclusions reached by Dr. Thiele and Professor Fletcher are completely supported by the testimony of many witnesses familiar with the creek long before Bagdad did any pumping. These witnesses, many disinterested, testified the creek uniformly dried up and the water disappeared usually about July each summer except in places where it reappeared at the surface including uniformly with the exception of two years, at Kingman Crossing. (14248 R. 142, 143, 144, 145, 150, 151, 155, 173, 174, 175, 178, 179, 180, 234, 235, 236)

Indeed, Zannaras himself, when his claim related to pollution and not shortage, so testified twice to this effect under oath. (14248 R. 411, 390)

## ANSWER TO ARGUMENT

### "BURDEN OF PROOF"

The rule is now established that "He who seeks to have a judgment set aside . . . carries the burden . . ."

*Palmer v. Hoffman*, 63 S.Ct. 477, 318 U.S. 109, 87 L.Ed. 645 144 A.L.R. 719.

28 U.S.C.A. Sec. 2111

"But it is likewise settled that appellee may, without taking a cross-appeal, urge in support of a decree any matter appearing in the record, although his argument may involve an attack upon the reasoning of the lower court or an insistence upon a matter overlooked or ignored by it."

*United States v. American Ry. Express Co.*, (1924) 265 U.S. 425,435

The appellants assume that the trial court affirmatively reached the conclusion which he did by application of the rule that the appellants had the burden of proof in establishing that the pumping operations of Bagdad rather than natural conditions caused a claimed shortage at appellants' diversion point. The record does not require any such conclusion. Rather it requires the conclusion that the trial court applied the rule

"A party who bases his right on prescription or adverse possession, or on the abandonment or forfeiture of prior rights, has the burden of proof as to such matters; but when he makes a prima facie showing, the adverse party has the burden of rebutting or overcoming it."

93 C.J.S. 1014, 1015, Sec. 201

67 C.J. 1061, note 19

Appellants' total appropriative right of 3,000,000 gallons annually is equal to 10 acre feet of water per year. (R. 471) There is no provision in the certificate of water right that appellants are entitled to this relatively small amount of water pro rata per day, per week or per month. (Plf's Ex. A in Evid. 14248 R. 22) The record is replete with evidence to the effect that it is a wasting stream in the summer, tending to disappear in the gravels and reappear from place to place. (14248 R. 142 et seq.; 150 et seq.; 173 et seq.) There is a gravel overlay at the Zannaras diversion by actual measurement and calculation varying from 7 feet to 37 feet. (R. 397, 398) These gravels carry a substantial amount of flow (R. 431) which could be made available. (R. 431, 632, 633, 634)

By Zannaras' own sworn statements made prior to development of his shortage claims he knew the creek historically dried up and wasted away in the summer. "I have known that there are seasons of the year when there is no running water to be seen in Burro Creek." (14248 R. 411) "No; this time today we have a very dry spell along there. It is now dry this time of the year." (14248 R. 390)

Apparently, even though Zannaras knew there were areas of the river bed which showed no live water in dry periods it is appellants' theory that a point of diversion could be established at a point where the gravels were relatively thick as immediately above the Zannaras diversion (R. 397, 398) where the record shows they were 37 feet deep as compared to an average depth of 10 feet for the channel, and, despite the fact it was well known that the water, in times of shortage would sink into these gravels, nonetheless insist that the entire flow of the creek be wasted on the chance that a few dribbles of water would thereby be forced to the surface. Such is not the public policy governing water use in the West.

" . . . The wasteful methods so common with early settlers can, under the light most favorable to their system of use, be deemed only a privilege permitted merely because it could be exercised without substantial injury to any one; and no right to such methods of use was acquired thereby."

*Hough v. Porter*, 98 P. 1083, 1102 (Ore. 1909)

*Raymond v. Wimsette*, 31 P. 537, 540 (Mont.)

*Fenstermaker v. Jorgensen*, 178 P. 760, 763 (Utah)

*Albion-Idaho Land Co. v. N.A.F. Irr. Co.*, 97 F. 2d 439

Upon the same theory, appellants could have initiated their appropriation a short distance below the Bagdad diversion where the water generally disappeared beneath the gravels other than under optimum water supply conditions and then insisted that Bagdad abandon in practical effect its appropriation except when a large amount of water was flowing in the creek, since, while the water was there if any effort were made to expose it through-



out the year in ample quantities nonetheless since it wasn't on the surface, therefore Bagdad must quit pumping even though such cessation would in no manner operate to bring the water to the surface. The great weight of the evidence was to the effect that this physical condition obtained below the Bagdad diversion. (14248 R. 149, 162, 163 Ex. B in Evid.)

The Court in its Memorandum decision (R. 31, 32) in effect found that *upon all the evidence* admitted, the Court could not justify a finding that Bagdad's pumping deprived appellants of water legally theirs. This is no "burden of proof" question—this is a finding by the Court, based on all the evidence, that the Court could not conscientiously make a finding necessary to warrant injunctive relief. Perhaps expressed in a backhanded manner but nonetheless expressed.

This is shown by the affirmative positive findings of fact formally made by the Court (a) that Burro Creek is a seasonal stream which wastes away or tends to waste away through the summer months; (b) that immediately below the Bagdad diversion Burro Creek spreads out into a long flat basin of 1374 acres overlaid with a heavy deposit of sands and gravels substantially overgrown with vegetation resulting in a very high loss of water from evaporation and transpiration during the summer months. (R. 33, 34)

The Court then found from all the evidence, *including the testimony as to annual summer water disappearance* long before Bagdad did any pumping of water below the Bagdad diversion that the Court could not find that the water shortage was attributable to Bagdad's pumping. By way of illustration:

John M. Neal, a cattle rancher with mining interests of Mohave County (owner of a 9,000 acre, 800 to 1,000 head of cattle ranch) who at 12 years of age had first hauled water from Burro Creek at the Zannaras diversion point and who from then on until 1929 was intimately acquainted with the area testified that he bought the Bogle, Olaya and Ferguson ranches in 1907 eighteen miles up the creek from the Bogle ranch headquarters and fifteen miles down the creek and owned them until 1929. During this

entire time he was personally familiar with conditions on the creek in this area. He testified that the water uniformly disappeared except where bed rock came to the surface to form a barrier every summer generally in July. (14248 R. 142, 143, 144, 145, 150, 151) (On cross examination):

"Q. You don't know, or do you know whether or not there was water flowing past the Zannaras point of — where he takes water out for his mill except in those two years that you mentioned?

"A. I saw the water flowing there many times up until June and sometimes the first of July before it would sink there.

"Q. What years are you talking about now?

"A. Well, any year from 1907 to 1929."

(14248 R. 151)

See also: Testimony of Orville Bogarth, Sheriff of Yavapai County, who rode the area from the age of 8 to 21; (14248 R. 155 et seq.); Ernest Degen, who prospected the area from 1905 for over 30 years (14248 R. 173 et seq.); A. D. Richardson, familiar with the area from 1923 on (14248 R. 178 et seq.); Alvis M. Short, a miner from Kingman, Arizona, familiar with the creek, particularly between 1925-1940. (14248 R. 234 et seq.)

Each of these witnesses testified from personal knowledge, unequivocally, that the creek below the Bagdad diversion dried up, other than for floods, potholes and where bed rock brought the underflow to the surface, every summer.

When there is then superimposed upon this unimpeached and dependable testimony the scientific study made by Dr. Thiele and Professor Fletcher, the rule as to burden of proof loses all significance for it is most clearly apparent that whatever the applicable rule may be, appellee not only proved the fact that its pumping in the summer is not the real cause of the shortage of water of which the appellants complain but demonstrated it so effectively that the result reached by the Court must be conceded

to have been a correct result whatever reasons may have been given for reaching it.

### ANSWER — "RES JUDICATA"

Counsel would, apparently for the purpose of this argument, consider Cause No. 321 as consolidated with No. 221 and for other purposes regard them as separate causes. "This cause (No. 221) is in no way dependent on Civil Cause Number 321." (R. 25)

However, we need not concern ourselves further with the many authorities cited by appellants since the situation is clearly governed by three separate and well-established legal principles.

This is clear for the reason that while the two causes had been under consideration by the Court, concurrently with its minute order finding the issues in Cause No. 321 for the defendants there and appellants here, the Court, by a further minute order vacated the order taking Cause No. 221 under submission specifically for the purpose of hearing further evidence. We respectfully submit that there could be no clearer evidence of the fact the Court reserved this issue for determination than its action in vacating the submission order in Cause No. 221, since the sole issue in Cause No. 221 was this question.

50 C.J.S. Sec. 659, p. 104 et seq.

"An order or judgment of a court is not final if an issue of law or fact essential to the disposition of the action is reserved for judicial determination."

*Restatement of the Law, "Judgments,"* Sec. 41, p. 161

*N.L.R.B. v. Clark Bros. Co.*, 163 F. 2d 373 (C.C.A. 2)

30 *Am. Jur.* Sec. 181, p. 927, "Judgments"

Second: Where two inconsistent judgments are rendered between the same parties, the last in time controls.

*Restatement of the Law, "Judgments,"* Sec. 42 p. 164 et seq.

49 C.J.S., Sec. 445, p. 876

*Donald v. J. J. White Lbr. Co.*, 68 F. 2d 441 (C.C.A. 5)

Either that or the later inconsistent judgment "setteth the matter at large."

49 C.J.S., Sec. 445, p. 876

*Kahl v. Chicago Title & Trust Co.*, D.C. Ill. 299 F. 793

Thirdly, and conclusively:

"... A sufficient answer is that neither by pleadings nor evidence were the proceedings in this other case brought before the court of claims in the present suit. If a party neither pleads nor proves what has been decided by a court of competent jurisdiction in some other case between himself and his antagonist, he cannot insist upon the benefit of *res judicata*, and this although such prior judgment may have been rendered by the same court. . . ."

*United States v. Bliss*, 172 U.S. 321, 43 L.Ed. 463, 465

50 C.J.S., Sec. 597, p. 15

*Murrell v. Stock Growers' Nat. Bank of Cheyenne*, 74 F. 2d 827, 833 (C.C.A. 10) (and numerous federal and state cases footnoted at pages 832, 833)

When the cause came on for further evidence March 9, 1954, appellants appeared and made no objection to taking of testimony and made no reference to the judgment in Cause No. 321. Appellee, before offering further evidence, outlined in detail its proposed further proof and no objection was made. (R. 347, 348, 349, 350, 351, 352, 353, 354) Appellants cross-examined all witnesses in detail and at length and at no time brought to the Court's attention or relied upon the judgment in Cause No. 321. Indeed, in appellants' "Renewal of Motion to Set Cause for Hearing" (R. 23 et seq.) filed December 5, 1953, the appellants flatly said "This cause is in no way dependent on Civil Cause Number 321." (R. 25) This was filed approximately three weeks after the Finding had been formally made by the Court in Cause No. 321.

We see no point in listing the many cases cited in *Murrell v. Stock Growers' Nat. Bank of Cheyenne* above referred to, since

the principle is accepted universally that a waiver follows failure to assert a claim based on a prior adjudication when such claim is relitigated in such subsequent litigation. Failure to assert the prior adjudication is universally regarded as an agreement to relitigate the issue since the defense of *res judicata* does not go to the jurisdiction of the court subsequently hearing the matter.

### "LAW OF THE CASE"

This portion of Appellants' Opening Brief seems to us entirely pointless for the reason that it is without application to the facts as they appear of record in this cause. The issues involved in Cause No. 321 are relatively simple. First, whether the certificate of water right was obtained by the defendants in that cause by fraud and whether or not such would warrant cancellation of the certificate. Secondly, whether the rights of the defendants in Cause No. 321 had been lost through forfeiture by nonuser. The court below held, and this Court affirmed the finding, that the statute of limitations denied plaintiff in that cause and appellee here the right to raise and litigate the issue of fraud and that there was sufficient evidence of *intermittent* use by defendants therein to prevent a statutory forfeiture. It is true that one of the defenses in that cause was that the pollution of the water by Bagdad and Bagdad's use itself of the water was an excuse for the defendants' failure to use the water and that the Court collaterally made a finding to the effect that a main cause of appellants' non-user was use by Bagdad. However, the fact that the Court was not satisfied with this evidence to the extent it was willing to order a perpetual injunction clearly appears from its order made concurrently with its order finding the issues for defendants in Cause No. 321 vacating the order of submission in Cause No. 221 for the taking of further evidence.

To lay once and for all the "ghost" of consolidation urged as a fact by appellants seeking to apparently by repetition convince the Court that Cause No. 321 and Cause No. 221 became merged and tried together, we make reference to the record in Cause No. 321 as appears in Cause No. 14248.

Referring first to the colloquy between court and counsel, one line of which appellants cite at page 40, in which the Court seeks to question why the causes should not be consolidated, it affirmatively appears that Bagdad at that point explained to the Court why consolidation would be improper, inasmuch as the issues and evidence would be different in the two causes. Following this colloquy at page 54 the Court states:

"Well, you go ahead with your 321. Then we will see."

to which remark appellants' then counsel stated: "221." The Court then replied "Yes, 221. Then we will see how it fits in."

The record discloses at page 141 that appellants' counsel at the conclusion of his case announced "We now rest our case on the Petition for Relief."

The minutes appearing in the transcript in Cause No. 14248, page 26 show the following:

"It is ordered that the plaintiffs in Civil 221 Prescott proceed with proof therein prior to presentation of evidence in Civil 321 Prescott."

"Hearing is now had on said Amended Petition for Relief in Civil 221 Prescott".

At the end of plaintiff's case as so labeled in the minutes, appears following the notation of the fact that plaintiff rested on the Petition for Relief in Civil 221 Prescott, the opening notation "Bagdad Copper Corporation's case."

It is unfortunate when counsel, in an effort to cooperate and conserve the time of opposing counsel and the Court, finds this willingness to cooperate apparently turned against it in an effort to show that the very harm which was brought to the Court's attention as the reason for not consolidating would now apparently nonetheless be inflicted upon appellee's position.

The law of the case is completely inapplicable in that first, the trial court did not regard the trial and findings made by it in Cause No. 321 as applicable to the issues in Cause No. 221 and

reserved the right to further explore the facts and the law in Cause No. 221. All this Court did on appeal was to conclude that the statute of limitations was applicable and the finding of the trial court with respect to intermittent use supported by evidence sufficient to sustain it. The conclusion stated that the judgment of the District Court in Cause No. 221 "nullified, impeached, reversed and overruled the former judgment and misconstrued and failed to carry out the mandate of this Appellate Court" evidences a complete lack of understanding of the issues in Cause No. 321 and Cause No. 221. Since the decision of this Court in Cause No. 321 we have not questioned the fact and do not now question the fact that as of the date of the decision of this Court the right of appellants to 3,000,000 gallons of water annually was established as a matter of law. That is the total insofar as this case is concerned that was there established. We see no point in extensively further replying to this phase of Appellants' Opening Brief.

### "PRIMA FACIE CASE"

Frankly, we are not entirely clear as to just what appellants are seeking to persuade the Court of in this phase of their brief. Apparently some point is made of the fact that a paper entitled "Renewal of Motion to Set Cause for Further Hearing" was filed, making certain representations to the Court and that Bagdad did not object to the matter being set. We are not aware of any rule which in effect makes an order to set an application for hearing an adjudication of the representations made in the motion to set or which requires a formal reply to a motion to set containing fact averments, denying the same. We find no law to that effect and presume the reason is there is none, for no one has ever before made such a contention.

We are quite sure that the assertion made by appellants at page 43 of their Opening Brief to the effect that Bagdad had never, prior to 1954, urged that water would not reach the Zannaras diversion point even if Bagdad did not pump any water, stems from a failure to have read the record carefully. We are

certain appellants do not seek to mislead the Court in this respect. A very substantial part of the testimony presented in the trial of Cause No. 221 on the setting of the Petition for Further Relief was directed to this very point. As we have before indicated the most comprehensive and convincing testimony was offered by John M. Neal of Kingman, Arizona, who prior to the turn of the century, as a boy hauled water for his father, who was mining in the area, from substantially the present point of diversion of Zannaras. Subsequently in 1907 he purchased the ranches which encompassed the entire stretch of the creek the situs of this controversy and he ranched there until 1929. It was clear in his testimony that uniformly about July of each year the water would fail. He was not shown to have any interest in this litigation or to have any connection with Bagdad and his testimony was entirely unimpeached. In this he was collaborated by the then Sheriff of Yavapai County, who rode the area as a cowboy in his youth and by numerous persons who had prospected the area for many years before Bagdad pumped any water from Burro Creek. Reference has been heretofore made in this brief, *supra*, page 24, to this testimony.

Appellants then attempt to distinguish the *Albion-Idaho Land Company case*. Their argument in this attempt is directed to phases of the holding in that case which have nothing to do with this case and hence do not reach the legal principle which the trial court felt was governing. In addition, there are of course numerous additional cases, several of which we cited, *supra*, page 22.

The record is made up of the long history of water failure every summer in Burro Creek, supported, bolstered and explained by the studies made of the area by Dr. Thiele and Professor Fletcher, which present as clear and convincing a showing as we believe could be made other than by putting on witnesses to repeat statements made by witnesses theretofore on the stand. The force of the evidence contrary to this was very weak and no attempt was made to disprove the scientific conclusions of the two expert witnesses. We therefore say that had the Court deter-



mined the case otherwise we would have felt completely confident that upon a review by this Court the conclusion would have been reached that there was no reasonable conclusion to draw other than that the failure of the water to reach the Zannaras point of diversion was directly related to the soil conditions and topography and not to the relatively small amount of water pumped by Bagdad. When it is realized that the maximum capacity of its pump was 94 acre feet per month if operated continuously this would amount to substantially 3 acre feet a day, which 3 acre feet otherwise would have spread out into an alluvial plane overgrown with phraetophytes, filled with sand and gravels and with a relatively insignificant slope under climatic and altitude conditions would, by calculations based on findings of the U.S.G.S. for that area lose in the month of June by evaporation and transpiration at least three-fourths of an acre foot of water for each acre in the area.

#### "CHANGE OF METHOD AND MEANS OF DIVERSION"

If we understand appellants correctly, it is their contention that when Bagdad, through a dam across a canyon adjacent to its mill, conserved and saved the tail water, permitting it to settle so the water could be reused, it made a change in its method of diversion, to the prejudice of appellants. It has been so long established as the water law of the West that he who salvages water may reuse it and that the premium is on the careful use and reuse of water and not upon its wasteful use, that we are mildly astounded at the contention. Apparently as a method of proving how much water Bagdad would have wasted had it not salvaged its tailings and reused the water, counsel proceeds to determine how much water Bagdad could pump and concludes that since it could pump the water it must have been there and then concludes that since Bagdad was milling generally 3,000 tons of ore per day it must have used 7,000 tons of water which would have returned to the creek.

Counsel then argues that because a witness testified that in 1944 Bagdad filed a notice of complete application of water to

beneficial uses showing beneficial use of 600,000,000 gallons of water per annum, therefore, even though nowhere else in the record does any evidence appear to support the fact it did or does use such water, nonetheless it is within the realm of propriety that this figure be used to prove how much water was used, for what purposes we do not know. Counsel next argues because the pump capacity of Bagdad was 394,000,000 gallons of water therefore it pumped this water and therefore if it pumped this water it would have let a lot of waste water run back to the stream if it hadn't salvaged it and therefore some type of legal damage resulted to Zannaras through Bagdad's salvaging its tailings water. The following selection of cases sets forth the law with respect to the use of salvage water and the rights of he who salvages it.

*Pomona Land & Water Co. v. San Antonio Water Co.*, 152 Cal. 618, 93 P. 881 (1908)

*Wiggins v. Muscupiabe L. & W. Co.*, 113 Cal. 195, 45 P. 164 (1896)

*Smith v. Duff*, 39 Mont. 382, 102 P. 984 (1909)

*Spaulding v. Stone*, 46 Mont. 483, 129 P. 327 (1912)

*Reno v. Richards*, 32 Ida. 1, 178 P. 81 (1918)

*Basinger v. Taylor*, 36 Ida. 591, 211 P. 1085 (1922)

*Hill v. Green*, 47 Ida. 157, 274 P. 110 (1928)

*St. John Irrigating Co. v. Danforth*, 50 Ida. 513, 298 P. 365 (1931)

*Ironstone Ditch Co. v. Ashenfelter*, 57 Colo. 31, 140 P. 177 (1914)

*San Luis Valley Irrigation Dist. v. Rio Grande Drainage Dist.*, 268 P. 533 (Colo. 1928)

*Coryell v. Robinson*, 194 P. 2d 342 (Colo. 1948)

"ADMITTED USE OF MORE WATER THAN ENTITLED TO USE UNDER CERTIFICATE OF WATER RIGHT"

## "USE OF WATER FOR PURPOSES OTHER THAN ITS OWN MINING OPERATIONS"

The foregoing two portions of appellants' brief merit only this reply. Dr. Thiele testified that if Bagdad pumped its rated 94 acre feet per month it would use approximately 1,100 acre feet of water per year. In this same testimony he called attention to the fact that in June Bagdad pumped only 69 acre feet, and the record is replete with references to the fact that in many instances the pumps were not the cause of insufficient water supply.

The use of water by Bagdad for uses other than mining is inconsequential and largely related to its mining operation as a related use. We do not believe the matter is of consequence justifying further reply.

## "FINDINGS OF THE STATE ENGINEER"

Again, this is the first instance we have encountered of the casual testimony of a witness who happened to be the Engineer of the State Water Department giving in effect adjudicatory force to his testimony. He stated no more, as a reading of the record will show, than that he, at the solicitation of Zannaras, went to certain points on the stream and that it was dry. He did not attempt to state he made any engineering study or that he went there in his capacity of State Engineer. In fact, there is no statutory authority authorizing any such activity on his part or giving to his observations, when as a matter of courtesy he visits a section of the state, the force of an official finding.

## "THE JUDGMENT IS CONTRARY TO THE WEIGHT OF THE EVIDENCE"

Appellants here seek to go behind the judgment rendered on the first trial of Cause No. 221 March 3 and 4, 1949, and to bring to the attention of the Court exhibits there introduced. In the hopes perhaps of justifying this, counsel refers to the first trial as a preliminary hearing and to the trial in 1952 and 1954 as the final hearing.

The facts are that the first judgment became a final judgment and appellants are not entitled to or justified in attempting to go behind it and in effect review that judgment on an appeal initiated some eight or nine years after the judgment became final.

The most interesting portion of this argument appears at pages 62 and 63 wherein counsel proves that Burro Creek is a continuously running stream by first taking the capacity of Bagdad's pumps, the testimony of witnesses as to the amount of water which could be pumped if the pumps were operating continuously and then concludes from these figures that in order for this equipment to operate successfully the stream has to be constantly flowing and therefore it must be flowing. At pages 65 and 66 counsel attempts by fragments of testimony to draw the conclusion that the testimony of Dr. Thiele and Professor Fletcher was based upon other than personal observation and facts known to the witness. The answer to that is that Dr. Thiele and Professor Fletcher both testified to a personal physical examination of the area with that of Dr. Thiele extending over the better part of two weeks assisted by four to six persons. Appellants then attack his testimony on the basis that apparently because water is found flowing at Kingman Crossing practically continuously, therefore Dr. Thiele's conclusion that water permitted to enter the upper end of the basin would not reach the lower end must be disbelieved. In this appellants demonstrate their lack of understanding of hydrology and of the testimony of Dr. Thiele. By his own physical examination he determined that the water level at the well at the Bogle Ranch approximately half way between the Bagdad diversion and Kingman Crossing was 150 inches higher than the lip of the bed rock at Kingman Crossing. This would be something over 12 feet higher. It is a well-known and simple principle of physics and hydrology that water generally seeks its own level. We would of necessity conclude that the only force which prevented the draining down of this water level with a rush to the lip of the bed rock at Kingman Crossing was the friction of the sand and gravels intervening limiting its movement in relation to the permeability of the material through

which it moved. Certainly, through the entire summer until the water level in the entire basin was drained down to the level of the outflow at Kingman Crossing there would be a return flow coming from the ground water at Kingman Crossing. This does not demonstrate that putting in water at the upper end of the basin at a rate slower than the basin was losing water during the hot summer months would in any fashion augment or increase the flow at Kingman Crossing. Counsel overlooks entirely the fact that there is no conflict in the evidence but that during the summer months the stream intermittently sinks beneath the surface and rises and that it generally disappears beneath the sands and gravels of the basin some few hundred feet below the Bagdad diversion, reappearing, it is true, from time to time. However, when the water is once underground it is apparent that the outflow which is seen at a point lower down on the stream is not the water which disappeared upstream shortly theretofore but is ground water which has been in the ground many days and which comes to the surface at that point by reason of geological conditions bringing it to the surface. Water does not "run" underground in the usual acceptance of that term—it moves underground.

### "WATER RIGHT A PROPERTY RIGHT"

We have no quarrel with this principle. Nor do we quarrel with the fact that this Court confirmed the water right of appellants to 3,000,000 gallons per year without, however, determining when such water was to be taken by appellants. Certainly, if appellants had a bona fide desire and need for water in a bona fide milling operation, knowing by their own sworn testimony heretofore referred to, that historically the creek dries up in the lower reaches through the hot summer months they would either have arranged to mill during the times of plentiful water or arranged a very simple storage basin wherein water, in times of plenty, might be stored against the shortages of the summer just as Bagdad has done. 10 acre feet of water is a relatively minor amount, so that the amount needed in storage to take care of the

relatively brief period of shortage in the summer would not be great. Certainly, too, it is significant that appellants have made no effort to tap the water moving in the gravels at their point of diversion. The testimony was uniform in the 1952 hearing that there was always water flowing at Kingman Crossing which means that the underground storage between there and the Zannaras diversion was under constant recharge. This testimony, coupled with the testimony of Mr. Dickie and Dr. Thiele heretofore referred to, conclusively demonstrates that there would be water available without serious expense to appellants even during the dry summer months if any reasonable effort was made to reach it. Indeed, one of their own witnesses so testified in the 1952 trial. (14248 R. 127)

We recognize that a lower senior appropriator may not be required to go to large expense to continue enjoyment of his water right. This does not mean, however, that where the nature of the stream is such that he must have reasonably foreseen that at certain periods of the year extra efforts would be required to reach the flow if use was to be made consistently, that such senior appropriator can refuse to make such reasonable effort. Zannaras by his own sworn testimony knew that such was the nature of Burro Creek.

## CONCLUSION

Bagdad respectfully asserts that it clearly and with convincing force demonstrated that the shortages occurring during the three hot summer months occur by reason of natural conditions and not by reason of its pumping activities. No real effort was made by appellants to contest such fact.

The natural conditions here are such that the underflow of the basin below Kingman Crossing must be tapped if a consistent supply of water is to be made available to Zannaras; either that or the milling operations should be tailored to the times when nature is kinder in its draughts upon the stream than through the hot summer.

We respectfully urge that the judgment of the District Court achieves a just and lawful result and should be affirmed.

Respectfully submitted,

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No. 15640

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IN THE  
United States  
Court of Appeals  
For the Ninth Circuit  
1957 TERM

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JOHN PHILLIP ZANNARAS,  
J. P. ROBINSON, JR. and  
U. S. TUNGSTEN  
CORPORATION,

*Appellants,*

vs.

BAGDAD COPPER  
CORPORATION,  
a Corporation,

*Appellee.*

Appeal from the  
United States  
District Court  
for the District  
of Arizona.

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BRIEF OF APPELLANTS

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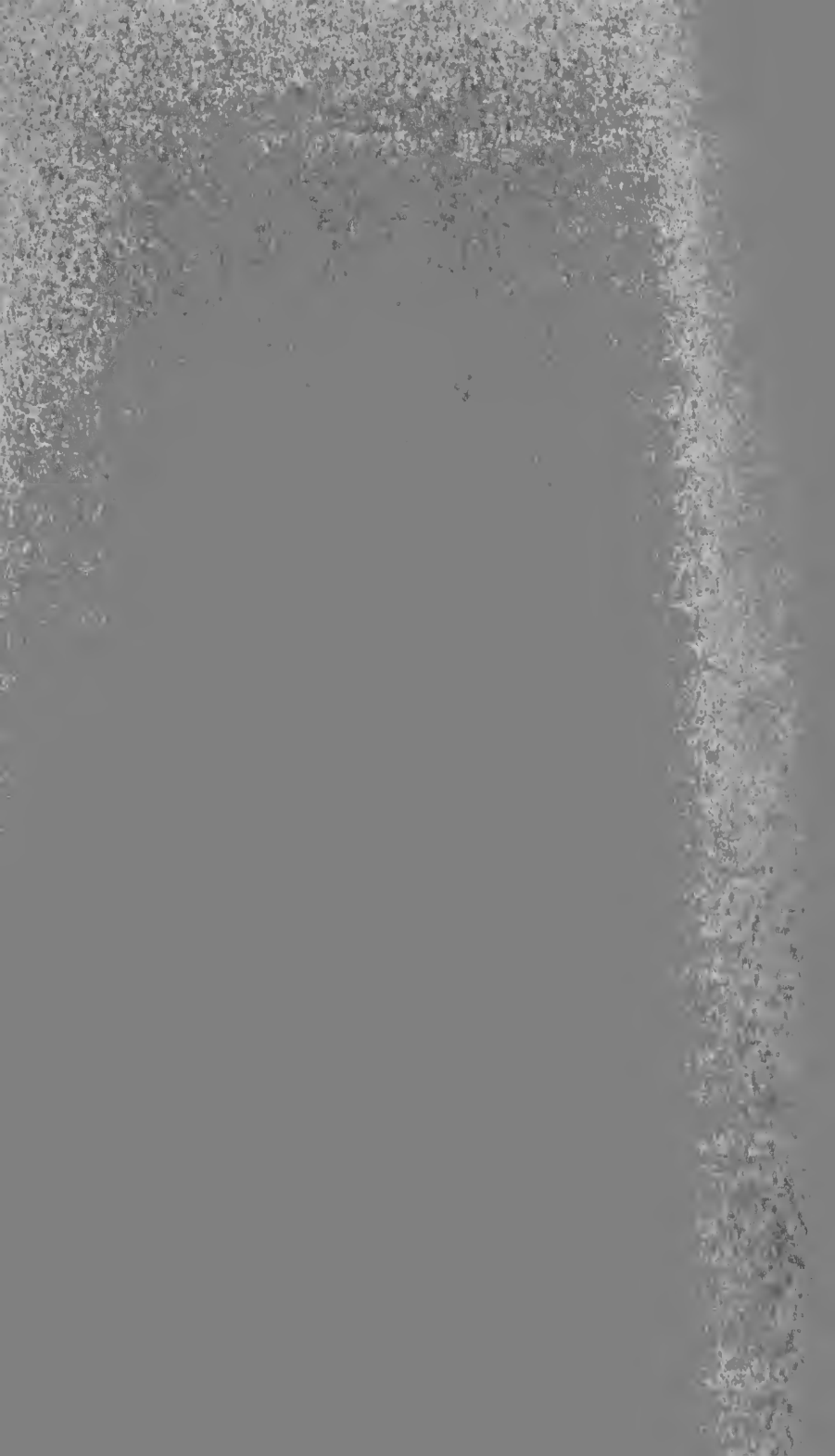
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3	R. 50	R. 52
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5	R. 50	R. 53
6	R. 50	R. 53
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(cont'd.)

## 1952 Trial

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10		14248 R. 109
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AB	R. 514	R. 561
AC	R. 578	R. 580
AD	R. 578	R. 580
AE	R. 607	R. 609

IN THE  
United States  
Court of Appeals  
For the Ninth Circuit  
1957 TERM

JOHN PHILLIP ZANNARAS,  
J. P. ROBINSON, JR. and  
U. S. TUNGSTEN CORPORATION

*Appellants,*

vs.

BAGDAD COPPER CORPORATION  
a Corporation,

*Appellee.*

No.  
15640

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BRIEF OF APPELLANTS

For the purpose of clarity, John Phillip Zannaras, J. P. Robinson, Jr. and U. S. Tungsten Corporation, an Arizona corporation, Plaintiffs in the District Court and appellants herein, will hereinafter be referred to as Zannaras-Robinson, and Bagdad Copper Corporation, a Delaware corporation, Defendant in the District Court and appellee herein, will hereinafter be referred to as Bagdad.

Reference to the printed Transcript of Record will be indicated by the letter "R" followed by the page number. Reference to the printed Transcript of Record

in Cause No. 14248 of this Court which has been ordered to be a part of this record on appeal will be indicated by "14248", the letter "R" and followed by the page number.

## JURISDICTION

The above entitled proceeding arises upon an appeal from a judgment entered in an initial action by John Phillip Zannaras and J. P. Robinson, Jr., residents and citizens of the State of Arizona, against Bagdad Copper Corporation, a Delaware Corporation. (Civil Cause No. 221.) During the course of the trial on May 13, 1952, on motion of counsel for John Phillip Zannaras and J. P. Robinson, Jr., the U. S. Tungsten Corporation, an Arizona corporation was added as a party plaintiff. (Docket entry May 13, 1952 R. 643-644.)

By their complaint filed July 12, 1948, (R. 3) Zannaras-Robinson pled their priority to the use of water from Burro Creek for their mining operations by reason of a certificate of water right issued by the Arizona State Land Department with a priority date of August 27, 1940, for the use from Burro Creek of 3,000,000 gallons of water per annum, in accordance with the terms of said certificate, alleged that the use of water by Bagdad, a junior appropriator upstream from Zannaras-Robinson, was depriving Zannaras-Robinson (downstream prior appropriators) of water to which they were entitled. An injunction was sought, requiring Bagdad to allow sufficient water to pass Bagdad's upstream point of diversion so as to allow Zannaras-Robinson to have the full use and enjoyment of the Zannaras-Robinson prior water rights, and enjoining and restraining Bagdad from interfering therewith. Damages were also sought amounting to \$1,500.00 per day from June 28, 1948, until such time as Bagdad ceased to interfere with the water rights of Zannaras-Robinson.

A motion for leave to amend complaint was filed October 18, 1948, (R. 9-10) and the motion was granted. (Docket entry R. 639).

The action was tried by the District Court sitting without a jury, on March 3rd and 4th, 1949, (R. 38 to 346). After trial the District Court, on March 27, 1949, by minute order, (R. 640) found that "Ptfs having failed to prove the allegations of their Complaint by a preponderance of the evidence, Order that judgment will be entered for the defendant herein." Over the objection of Zannaras-Robinson, Findings of Fact, Conclusions of Law and Judgment was entered January 2, 1951, denying relief to Zannaras-Robinson but retaining jurisdiction. (R. 12)

In accordance with the interlocutory order of the District Court, Zannaras-Robinson filed a petition for relief February 8, 1951 (R. 13-16), alleging continued deprivation of water by Bagdad, which was amended on March 28, 1951. (R. 18-21). Trial was had on the amended petition for relief after the District Court consolidated for trial this action (Civil Cause No. 221) and Civil Cause No. 321, entitled Bagdad Copper Corporation, a corporation, Plaintiff, vs. John Phillip Zannaras and J. P. Robinson, Jr., Co-partners, and U. S. Tungsten Corporation, Defendants. This latter case, Civil Cause No. 321, was decided by the District Court on November 12, 1953 (14248 R.) and affirmed by this Appellate Court on January 30, 1956, being cause number 14248 of this Court. (229 F 2d 920).

Based upon the opinion of this Appellate Court in Civil Cause No. 14248, reported in 229 F. 2d 920, involving the same parties, determining the same water rights, plus the fact that supporting evidence for both cases was adduced at the same hearing when the two actions were consolidated for trial, this appeal seeks enforce-

ment of the mandate of this Appellate Court decreeing the water rights of the parties. Jurisdiction is therefore asserted on this basis among others.

Upon the completion of the taking of testimony on May 14, 1952, both cases, Civil Causes No. 221 and 321, were submitted to the District Court. The District Court rendered a decision in Civil Cause No. 321 (not this case on appeal) on November 12, 1953, entering judgment in favor of the defendants John P. Zannaras, J. P. Robinson, Jr. and U. S. Tungsten Corporation, and against the plaintiff Bagdad Copper Corporation. The judgment in Civil Cause No. 321 was appealed to this Court and affirmed on January 30, 1956, in Circuit Court Cause No. 14248, (229 F 2d 920).

On December 5, 1953, and prior to the affirmation of the judgment in Civil Cause No. 321, Zannaras-Robinson filed a Renewal of Motion to set this cause for hearing (Civil Cause No. 221). (R. 23-25). Hearing was had before the Court. The District Court, by memorandum, filed March 29, 1957, determined that "Plaintiffs having failed to prove by a preponderance of the evidence that defendant has appropriated any of plaintiffs' water, they are not entitled to an injunction." (R. 32) Findings of fact and conclusions of law were submitted by Bagdad, and over the objection of Zannaras-Robinson, approved and settled by the Court, and judgment entered April 17, 1957, denying to Zannaras-Robinson any relief. (R. 32-35). Said judgment being diametrically opposed to the Findings of Fact, Conclusions of Law and Judgment theretofore rendered by the same District Court, involving the same parties, the same water rights and the same evidence in Civil Cause No. 321, (14248 R. 37-40), and affirmed by this Appellate Court as reported in 229 F. 2d 920.



The action is one between residents and citizens of different states and the amount in controversy exceeds \$3,000.00, exclusive of interest and costs. The jurisdiction of the District Court rested upon diversity of citizenship. 28 U.S.C.A. Sec. 1332.

The judgment having become final, the present appeal is predicated upon 28 U.S.C.A. Sec. 1291.

## STATEMENT OF THE CASE

### *Chronological History*

About June 1, 1940, John Phillip Zannaras and John P. Robinson leased the Mystery Gold mining claims, situated approximately 45 miles in a northwesterly direction from Congress, Yavapai County, Arizona (R. 41). They located a millsite alongside Burro Creek. Zannaras-Robinson proceeded building and operating a mill (R. 41), using water from Burro Creek for mining, milling and domestic purposes (R. 44). In the fall of 1941 Zannaras-Robinson located a group of tungsten mining claims (R. 88), proceeded to develop these claims, and entered into a 5-year contract with the U. S. General Services Administration, under which the Federal Government was to purchase their production (14248 R. 89, R. 637). Their mine was given the highest priority for materials and serialized by the Defense Metal Administration (14248 R. 90). They patented 8 mining claims and one millsite, and located and filed on 47 unpatented mining claims (14248 R. 353), spent \$250,000.00 on these properties up to the year 1952 (14248 R. 352), constructed a 250-ton mill, shipped ore to the Government stockpile assaying 1.92% WO<sub>3</sub> (R. 91), received \$4,000.00 for concentrates of tungsten shipped to Kennametal, Inc. (14248 R. 357) and custom milled ore for others. (14248 R. 236, 320).

Zannaras-Robinson applied for and received a Certificate of Water Right from the State of Arizona, with priority date of August 27, 1940, to divert and put to beneficial use for mining and domestic purposes 3,000,000 gallons of water from Burro Creek annually. (Ex. 1 1949 Trial, 14248 R. 22-24). Bagdad applied for and received a Certificate of Water Right from the State of Arizona, with priority date of November 4, 1941, to divert and put to beneficial use for mining purposes 315,360,000 gallons of water from Burro Creek annually. (14248 R. 397-400). It is significant to note that the application was for 600,000,000 gallons annually and was reduced by the State of Arizona Water Commissioner to 315,360,000 gallons annually. (14248 R. 304).

Burro Creek is a tributary of the Bill Williams River, which river in turn flows into the Colorado River. The Zannaras-Robinson point of diversion of water from Burro Creek is seven miles below the Bagdad point of diversion. (Ex. A 1952 trial and Ex. Q 1954 trial). Zannaras-Robinson are therefore the downstream prior appropriators, and Bagdad is the upstream junior appropriator. The Zannaras-Robinson mill is alongside Burro Creek, and their point of diversion is on Burro Creek (R. 40); the Bagdad mill is seven miles away from its point of diversion on Burro Creek.

Bagdad takes water from a sump at its point of diversion on Burro Creek which is a hole it has dug down fifteen feet below the surface of the natural bed of the creek. (R. 283). The Federal Government has installed gauges at that point to measure the amount of water flowing out of the sump after Bagdad has taken water for its use. (14248 R. 53).

This controversy over the waters of Burro Creek and the claim of damage by Zannaras-Robinson has been going on practically ever since late 1943, the time of the commencement of operations by Bagdad. In February 1945 Zannaras-Robinson brought suit against Bagdad, claiming that ever since December 1943 Bagdad had polluted and was continuing to pollute the waters of Burro Creek, making it impossible for Zannaras-Robinson, the downstream senior appropriators, to use the water to which they were entitled under their permit. Civil Cause No. 129, entitled J. P. Zannaras and J. P. Robinson, Jr. vs. Bagdad Copper Corporation, was filed in the United States District Court for the District of Arizona. After one day's trial, and prior to the commencement of the second day's trial, the parties, through their counsel, announced to the Court that a settlement had been reached whereby Bagdad agreed to pay and did pay Zannaras-Robinson the sum of \$1,000.00 as general damages and agreed to the issuance by the Court of an injunction against any further pollution by Bagdad of the waters of Burro Creek.

Early in the year 1945, which was about a year after the issuance of a water right to it by the State of Arizona (14248 R. 397), Bagdad rearranged the disposal of its tailings and its method of securing water, whereby its tailings disposal was removed from a position near Boulder Creek where water escaped back into Burro Creek, to a point three and one-half miles away, near the Bagdad Mill. Under the prior arrangement the tailings, containing 70% water (R. 172-176), escaped downstream with no chance of Bagdad reclaiming any of that water. Under the new arrangement Bagdad built a dam across an arroyo or wash, at the new tailing disposal location near the Bagdad Mill, and completely restrained the water from the Bagdad tailings from escaping into Burro Creek.

Bagdad admits it is pumping 1,100 acre feet of water which amounts to 358,436,100 gallons from Burro Creek per annum (R.471), which is in excess of the maximum amount that Bagdad can legally pump under its water right even if there was sufficient water in the creek after allowing water for Zannaras-Robinson as prior and superior downstream appropriators. This water according to Bagdad's own witnesses is used not only for Bagdad's own mining operation but is furnished by Bagdad to other mines in the vicinity and to persons living in the camp of Bagdad (R. 221, 222, 226), also in violation of Bagdad's water right.

This complaint (R. 3) was filed by Zannaras-Robinson on the 12th of July 1948 in the United States District Court for the District of Arizona, against Bagdad, alleging that Zannaras-Robinson were downstream prior appropriators being deprived of water to which they were entitled, by the illegal diversion by Bagdad, a junior upstream appropriator; they sought an injunction enjoining unlawful diversions and an order directing that sufficient water be let down by Bagdad to meet the needs of Zannaras-Robinson; they also sought damages of \$1,500.00 per day. Bagdad filed a general denial and, in defending this action in 1949, put on numerous witnesses, all of whom attempted to show that there was always the year around plenty of water at the Zannaras-Robinson point of diversion after the Bagdad diversions, and that therefore there was plenty of water for both diversions.

Without questioning the validity and priority of the Zannaras-Robinson water rights, the District Court, after trial, entered a minute order March 27, 1950, that "Ptf's. having failed to prove the allegations of their complaint by a preponderance of the evidence, Order that judgment will be entered for the defendants here-

in" (R. 640). Subsequently, on January 2, 1951, Findings of Fact, Conclusions of Law and Judgment was entered, over the objections of Zannaras-Robinson, denying relief to Zannaras-Robinson but retaining jurisdiction. (R. 12)

On February 8, 1951, Zannaras-Robinson filed a petition for relief in this same case (R. 13-16) based upon the retention of jurisdiction by the District Court, (as set forth in its Order dated January 2, 1951), which was amended March 28, 1951. (R. 18-21). Following the filing of the February 8, 1951 petition by Zannaras-Robinson for relief, Bagdad on March 5, 1951 filed a suit in the United States District Court for the District of Arizona, Civil Cause No. 321, entitled, Bagdad Copper Corporation, Plaintiff, vs. John Phillip Zannaras and J. P. Robinson, Jr., Defendants. (14248 R. 3-9). In Cause No. 321 Bagdad sought a "judgment decreeing and declaring that said Certificate of Water Right No. 1341 (The Zannaras-Robinson Certificate of Water Right) is void, and that the defendants (Zannaras-Robinson) have no rights thereunder, and decreeing and declaring that any rights which said defendants (Zannaras-Robinson) may have in and to the water of Burro Creek by reason of their (Zannaras-Robinson) said application of August 27, 1940, are no longer of legal force or validity and that the rights of plaintiff (Bagdad) in and to the waters of Burro Creek are superior to any rights of said defendants (Zannaras-Robinson) and quieting the rights of plaintiff (Bagdad) thereto; or decreeing and declaring in the alternative that defendants (Zannaras-Robinson) have no right in and to the water of said Burro Creek prior and superior to plaintiff's (Bagdad's) rights under its said application of November 5, 1941 in an amount in excess of one thousand gallons per year; together with such other and further relief as equity may require." (14248 R. 9) (Brack-

eted words within quotes supplied). The complaint further alleged that Bagdad was dependent upon the water which will be used by Zannaras-Robinson under their certificate of water right and that if the Zannaras-Robinson certificate was not voided that Bagdad would of necessity be forced to substantially lessen or close down its mining and milling operation, which would cause Bagdad a loss in excess of the sum of \$10,000 per annum. (14248 R. 5)

Zannaras-Robinson in answering the action filed against them by Bagdad denied the allegations, and answered defensively that Zannaras-Robinson were prior and superior certificated appropriators, that Bagdad, a junior and inferior appropriator, had, first by polluting, and later by drying up the creek, and thus depriving them of necessary water, made it impossible for Zannaras-Robinson to operate their mill, and further alleged that they could not economically operate their mill spasmodically. Zannaras-Robinson in the answer also pled affirmatively for an injunction enjoining Bagdad from interfering with water from Burro Creek to which Zannaras-Robinson, as prior and superior appropriators, were entitled. (14248 R. 10 et seq.)

In answering the Zannaras-Robinson Amended Petition for Relief, Bagdad filed a general denial, and in addition, (R. 22) pled by reference its complaint in Civil Cause No. 321 heretofore alluded to. (14248 R. 3-9)

Issue was joined on Civil Cause No. 221 (this case now on appeal), and on Civil Cause No. 321, the case mentioned in the foregoing paragraphs. The two cases (Civil Causes No. 221 and 321) were consolidated for trial and tried before the Court on May 13 and 14, 1952, on the same hearing. The evidence adduced at this

consolidated trial was applicable to both cases (Civil Causes No. 221 and 321) for matters involving the water rights of the parties hereto and the illegal deprivation by Bagdad of water to Zannaras-Robinson. These matters were expressly presented to and determined in favor of Zannaras-Robinson first by the District Court in Civil Cause No. 321 and affirmed by this Appellate Court in App. No. 14248 and reported in 229 F 2d 920.

It is significant that for this 1952 hearing Bagdad reversed its position in regard to water availability for the Zannaras-Robinson operation. In the 1949 trial heretofore alluded to, Bagdad, through its witnesses, attempted to convince the Court that there was always the year around plenty of water at the Zannaras-Robinson diversion point in Burro Creek after the diversion by Bagdad. In the trial in 1952 on the other hand, Bagdad, through its witnesses, attempted to convince the Court that the reason there was no water at the Zannaras-Robinson point of diversion in the summer months was because of the seasonal lack of water and not by reason of the pumping operations of Bagdad. This position was taken in the face of the Bagdad complaint in Civil Cause No. 321 (with which this cause on appeal was consolidated for trial) wherein Bagdad had, in its pleadings, alleged that if Zannaras-Robinson used the water to which they were entitled under their Certificate of Water Right, then the mining operations of Bagdad would be substantially lessened or that *Bagdad would have to close down*. We will later point out that even this reversed position was abandoned at the 1954 hearing.

Over the objection of Bagdad, findings of fact, conclusions of law and direction for entry of judgment, and judgment, were duly signed and filed November

12, 1953 in Civil Cause No. 321 (14248 R. 37 et seq.). The validity of the Zannaras-Robinson Certificate of Water Right was upheld, and findings of fact Number III found that : “\*\*\* For approximately five (5) months in each year, due mainly to plaintiff’s (Bagdad’s) pumping operations and use of water above, there was no water at the defendants (Zannaras-Robinson’s) point of diversion” (bracketed words supplied) (14248 R. 39), and specifically ordered and decreed in the formal judgment which was entered November 12, 1953, that Zannaras-Robinson “\*\*\* are the owners of and entitled to the prior use of three million (3,000,000) gallons of water annually from Burro Creek\*\*\*” and “\*\*\*have the right as prior appropriator, to take water from Burro Creek” \*\*\*“without interference by plaintiff’s (Bagdad’s) use above.” (14248 R. 41, 42). (Bracketed word supplied.)

That judgment of the District Court was appealed by Bagdad to this Appellate Court, being assigned No. 14248, and was affirmed January 30, 1956. (229 F 2 920). The question of Bagdad depriving Zannaras-Robinson of water was involved in both Civil Cause No. 221 and 321 which were tried in 1952 on the same evidence as to facts and law on the same hearing and appear on the same record, and also as to the right of Zannaras-Robinson to use water from Burro Creek without interference by Bagdad. These issues were expressly presented to this Appellate Court by Bagdad in its statement of points on appeal of Civil Cause No. 321, (14248 R. 433-436), and also in Bagdad’s brief on appeal. The judgment of the District Court was affirmed by this Court on January 30, 1956 (229 F 2 920) and a mandate dated March 2, 1956 directed to the United States District Court for the District of Arizona. Thereby this Appellate Court affirmed the prior right of Zannaras-Robinson to the use of 3,000,000 gallons of water per



annum from Burro Creek without interference by Bagdad. It also affirmed the finding of the District Court that the shortage of water at the Zannaras-Robinson point of diversion for five months of the year was due mainly to Bagdad's pumping operations.

Following the entry of judgment by the District Court on November 12, 1953 in Civil Cause No. 321 in favor of Zannaras-Robinson, and prior to the decision of the Appellate Court on that cause, Zannaras-Robinson filed, on November 18, 1953, a motion to set Civil Cause No. 221 (this cause on appeal) for further hearing, (R. 644) which was stricken from the calendar subject to renewal in the spring. (R. 644). On December 5, 1953 Zannaras-Robinson filed a Renewal of Motion to Set Cause for hearing. (R. 23-27). The object of this hearing is affirmatively shown on the face of the motion (wherein the judgment in favor of Zannaras-Robinson and against Bagdad in Civil Cause No. 321 was pleaded). The motion was granted without objection by Bagdad and hearing held by the Court in order to determine the character of judgment to be entered against Bagdad, without awaiting the then pending decision of this Appellate Court in Civil Cause No. 321 (App. No. 14248).

At the hearing of March 1954, Bagdad abandoned its former position that the reason there was no water at the Zannaras-Robinson point of diversion was because of the seasonal nature of the creek, and brought in expert witnesses to attempt to show by calculations, based upon hypothetical assumptions, that even though Bagdad diverted the entire flow of the creek during the summer months and part of the fall months, such diversion would have no effect upon the flow of water at the Zannaras-Robinson point of diversion as the water would have been lost by evaporation and transpiration.

In other words, Bagdad tried to relitigate facts and issue already adjudicated by the District Court in Civil Cause No. 321, which adjudication was then pending on appeal to this Appellate Court.

Upon the conclusion of the taking of testimony March 11, 1954, the case was submitted to the Court for decision. (R. 636)

In the meantime the decision of the District Court in Civil Cause No. 321 was affirmed by this Appellate Court (229 F 2d 920) on January 30, 1956, and thereafter a mandate was directed to the District Court. That decision was in favor of Zannaras-Robinson and against Bagdad. The judgment (14248 R. 37-43) decreed that Zannaras-Robinson were the owners of a valid Certificate of Water Right issued by the State of Arizona, entitling them to put to beneficial use 3,000,000 gallons of water per annum without interference by Bagdad's use above, and found that "For approximately five (5) months in each year, due mainly to plaintiff's (Bagdad's) pumping operation and use of water above, there was no water at the defendants' (Zannaras-Robinson) point of diversion." (Bracketed words within quotes supplied.)

Then on March 29, 1957, the District Court filed a memorandum on Petition for Relief. (R. 31). This memorandum is in part that, "The evidence submitted is not sufficient to enable the Court to find as a fact that during critical months of the year, even if Bagdad ceased its pumping operations, that water would reach the Zannaras point of diversion, and the rule announced in Albion-Idaho Land Co. vs. NAF Irr. Co. 97 F. 2d 439, would therefore appear to be applicable."

Thereafter, on April 17, 1957, Findings of Fact, Conclusions of Law and Judgment in favor of Bagdad and

against Zannaras-Robinson was signed, filed and docketed (R. 32-35) over the objection of Zannaras-Robinson.

### CONCISE STATEMENT OF POINTS

1. The District Court erred in ruling that Burro Creek is a seasonal stream, generally wasting away, or tending to waste away during the months of June, July, August, and on occasion, September, in each year, depending upon the rainfall on its water-shed, and that during the remaining months of the year there is generally adequate water in Burro Creek for all claims of both plaintiffs and defendant.

2. The District Court erred in ruling in favor of the upstream junior appropriator defendant and against the downstream senior appropriator plaintiffs based upon the evidence being "insufficient to enable the Court to determine whether the pumping by the defendant Bagdad Copper Corporation during seasons of scarcity has any bearing" on the amount of water reaching the downstream senior appropriator plaintiffs' point of diversion.

3. The District Court erred in ruling that if the evidence is insufficient to enable the Court to determine as a fact that the use of water by an upstream junior appropriator results in injury to a downstream senior appropriator an injunction will not lie.

4. The District Court erred in ruling that the burden of proof was upon the downstream senior appropriator plaintiff to prove that the admitted pumping operations of the upstream junior appropriator defendant resulted in damage to the downstream senior appropriator plaintiffs.

5. The District Court erred in its ruling denying the application of the downstream senior appropriator plaintiffs for an injunction restraining the upstream junior appropriator defendant from interfering with the right of the downstream senior appropriator plaintiffs to the beneficial use of 3,000,000 gallons of water per annum from Burro Creek, in accordance with the terms of plaintiffs' Certificate of Water Right.

6. The District Court erred in its ruling that the use of water from Burro Creek by the upstream junior appropriator defendant did not deprive the downstream senior appropriator plaintiffs of water at their point of diversion.

7. The District Court erred in its ruling that the admitted use by the upstream junior appropriator defendant of water from Burro Creek is not proved to be the reason for the lack of water at the downstream senior appropriator plaintiffs' point of diversion.

8. The District Court erred in its ruling in favor of the defendant and against the plaintiffs in that the matter of deprivation of water by the upstream junior appropriator defendant to the detriment of the downstream senior appropriator plaintiffs had already been adjudicated by the United States District Court for the District of Arizona (Cause No. Civ. 321—Prescott) and affirmed by the Circuit Court of Appeals for the Ninth Circuit (Cause No. 14248), 229 Fed. 2d page 920, entitled Bagdad Copper Corporation, a corporation, Appellant, vs. John Phillip Zannaras and J. P. Robinson, Jr., Co-partners, and U. S. Tungsten Corporation, Appellees, (the same parties involved herein), wherein ruling was made that the lack of water in Burro Creek for plaintiffs' use for 5 months of each year was caused by the upstream pumping by defendant.

9. The District Court erred in its ruling that the burden of proof was upon the downstream senior appropriator plaintiffs to show that the lack of water for plaintiffs' use was the result of the junior appropriator upstream defendant's pumping.

10. The District Court erred in ruling that the evidence adduced was insufficient to enable the Court to determine as a fact that the use of water by an upstream junior appropriator was the result of the injury to the downstream senior appropriator.

11. The District Court erred in ruling that the burden of proof is upon the downstream senior appropriator to prove as a fact that the cause of its injury was attributable to the admitted pumping operations by the upstream junior appropriator.

12. The District Court erred in ruling for the defendant when the District Court found that the evidence was insufficient to enable the Court to determine that the act of the upstream junior appropriator defendant resulted in the lack of water available for the downstream senior appropriator plaintiffs.

13. The District Court erred in ruling in favor of the defendant and against the plaintiffs in that such ruling is contrary to the weight of the evidence.

14. The District Court erred in ruling that the downstream senior appropriator plaintiffs are not entitled to an injunction against the upstream junior appropriator defendant.

15. The District Court erred in ruling that the plaintiffs are not entitled to an injunction against the defendant in that the denial is contrary to the findings and evidence on the file in the office of and testified to by the Arizona State Water Commissioner, an offi-

cial of the State of Arizona, charged by law with keeping records and making investigations.

16. The District Court erred in ruling against the plaintiffs and in favor of the defendant in that the burden of proof is upon one who changes its method and means of diversion to affirmatively show that such change in method and means of diversion will not damage downstream senior appropriator.

17. The District Court erred in denying relief to the plaintiffs when the defendant in its testimony asserted it was using large amount of water for purposes other than for its own mining operations.

18. The District Court erred in not granting the injunctive relief sought by the plaintiffs when the evidence clearly discloses that the diversions by defendant for 5 months each year is depriving the plaintiffs of water to which they are entitled.

19. The District Court erred in failing to find as a fact that the plaintiffs were the senior and the defendant the junior appropriators of waters of Burro Creek, as the evidence conclusively proved such to be true, and the priority had been previously adjudicated by the United States District Court for the District of Arizona (Cause No. Civ. 321—Prescott) and affirmed by the Circuit Court of Appeals for the Ninth Circuit (Cause No. 14248), 229 Fed. 2d page 920, entitled Bagdad Copper Corporation, a corporation, Appellant, vs. John Phillip Zannaras and J. P. Robinson, Jr., Co-partners, and U. S. Tungsten Corporation, Appellees, (the same parties involved herein.)

20. The District Court erred in not granting the injunctive relief sought by the downstream senior appropriator plaintiffs when the evidence clearly discloses that the amount of water used by the upstream junior

appropriator defendant exceeds the amount of water to which it claims to be entitled under its certificate of water right.

21. The District Court erred in failing to require the upstream junior appropriator to affirmatively and specifically plead and affirmatively prove by clear, convincing and satisfactory evidence that the admitted use of water by such upstream junior appropriator does not deprive the downstream senior appropriator of the amount of water to which it is entitled.

22. The District Court erred in denying the application of the downstream senior appropriator for injunctive relief against the upstream junior appropriator in that the effect of such denial deprives the downstream senior appropriator of property without due process of law and without the payment of just compensation therefor.

## ARGUMENT

This argument is urged in support of Concise Statements of Points Number 2, 3, 4, 5, 6, 7, 9, 10, 11, 12, 14, 16, 21.

## BURDEN OF PROOF

It is the position of Zannaras-Robinson that the burden of proof was upon Bagdad, as the upstream junior appropriator, to show by clear and convincing evidence that the admitted interception and diversion by Bagdad of some 1,100 acre feet (358,436,100 gallons) of water per year from Burro Creek did not affect the natural flow of the creek nor interfere with the right of Zannaras-Robinson as prior appropriators to use up to 3,000,000 gallons of water at their point of diversion.

In the well recognized work of Kinney on Irrigation and Water Rights, Second Edition, Vol. 3, Sec. 1640, page 3003, the following statement is found:

“Sec. 1640. Proof—Burden of Proof. In an action to enjoin the defendant from diverting water, or to prevent him from a continuous invasion of any of the plaintiff’s alleged rights, it devolves upon the plaintiff, in the first instance, to establish a *prima facie* case to his right to the use of the water or other right in question, as set forth in the allegations of his complaint, and also the essentials necessary, such as irreparable injury to his rights, before the Court will grant the injunction prayed for.\*\*\*”

And in the same section at page 3004:

“\*\*\*But, as a general rule, upon the plaintiff making out a *prima facie* case, the burden is then cast upon the defendant to show that he is entitled to the water claimed by him in accordance with the allegations of his answer. \*\*\**So, where the defendant seeks to justify his acts in taking the water under the allegation that it will not reach the prior appropriator and plaintiff below, even if permitted to flow down the stream, and will, therefore, be of no use to him, not only is the burden of proof upon such defendant to show that fact, but the evidence must be most clear and convincing.*\*\*\*” (Emphasis supplied.)

In support of the last statement underscored above, the case of Alamosa etc. Co. v. Nelson 42 Colo. 140, 93 Pac. 1112 is cited in support thereof. On page 1115 of the Pacific Report the decision of the court is:

“*Where a senior seeks to enjoin a junior appropriator of water from diverting the same to the injury of the former, and the junior appropriator seeks to avoid the same upon the ground that if the use which he threatens to make of it is restrained the owner of the senior right will derive no benefit, such a defense ought to be established by clear and satisfactory evi-*



*dence.* The infringement of a prior by the owner of a junior right constitutes a legal injury, and, before the junior can justify his acts of interference with the prior right upon the ground stated, a strong showing should be made. Upon this controverted issue of fact which the defendants have set up in their affirmative defense the evidence was conflicting, and the defense was not established to the satisfaction of the trial court. On the contrary, the evidence was legally sufficient to uphold its finding in plaintiff's favor, and we cannot interfere with it." (Emphasis supplied.)

Vol. 93 Corpus Juris Secundum, Waters, Sec. 201a at page 1015, in discussing presumptions and burden of proof, contains the statement:

“\*\*\*As against a prior appropriator, the adverse party may have the burden of proving that his storage or use of water does not interfere with the rights of the prior appropriator, as by proving that he has developed or is collecting, storing, or using water which, without his acts, would not reach the prior appropriator and be available to him under his appropriation.\*\*\*”

and in support of this statement cites:

Allendale Irr. Co. v. State Water Conservation Board, 113 Mont. 436, 127 P. 2d 227, Irion v. Hyde, 110 Mont. 570, 105 P. 2d 666.

Silver King Consol. Mining Co. v. Sutton, 85 Utah 297, 39 P. 2d 682.

DeHaas v. Benesch, 116 Colo. 344, 181 P. 2d 453.  
67 C.J. p. 1061 notes 25\* and 26\*\*

\*Donich v. Johnson, 77 Mont. 229, 250 Pac. 963;

Peterson v. Wood, 71 Utah 77, 262 Pac. 828.

\*\*Midway Irrigation Co. v. Snake Creek Mining & Tunnel Co. 271 F. 157 (Cert. granted 41 S. Ct. 536, 256 U. S. 687, 65 L. Ed. 1172, and aff. 43 S. Ct. 215, 260 U. S. 596, 67 L. Ed. 423); Greely and Loveland

Irrigation Co. v. Huppe, 60 Colo. 535, 155 Pac. 386; Jackson v. Cowan, 33 Idaho 525, 196 Pac. 216; Spaulding v. Stone, 46 Mont. 483, 129 Pac. 327; Rasmussen v. Moroni Irr. Co. 56 Utah 140, 189 Pac. 572; Mountain Lake Mining Co. v. Midway Irr. Co., 47 Utah 346, 149 Pac. 929.

Finding of Fact No. 5 is: "The evidence is insufficient to enable the Court to determine whether the pumping by the defendant Bagdad Copper Corporation during seasons of scarcity has any bearing upon the failure of the water flowing past its point of diversion to reach the point of diversion of plaintiffs due to the high rate of evaporation and transpiration."

The trial court's judgment in *Irion v. Hyde* supra (second appeal 110 Mont. 570, 105 P. 2d 666) was reversed by the Supreme Court of Montana. At page 673 of 105 P. 2d the court in its opinion stated;

"18. *In its sixth finding the court found that the evidence was insufficient to determine what volume of water at the defendants' premises would be necessary to reach plaintiffs' diversion in any useful quantity. Not only is that finding true, but the facts above recited indicate that no such evidence can possibly be given due to the four indeterminate and indeterminable variables mentioned above. We must, therefore, sustain appellants' objection to the further finding, added by the court about two months after the original findings and conclusions, to the effect that 'either party may, upon notice to the other, apply to the court for a further hearing to fix definitely what volume of water is necessary at defendants' premises to reach the point of diversion of the plaintiffs in any useful quantity.'*

"The evidence does disclose, however, that there may at times be conditions, such as empty pot holes, dry stream bed, and rainfall principally or entirely above defendants' dam and not long continued in character, under which it may be demonstrable that storage or

diversion by defendants may not be the proximate cause of plaintiffs' failure to receive water. *In such instances defendants have both the burden and the privilege of showing the facts; but it seems obvious that no general rule can be devised 'to fix definitely what volume of water is necessary at defendants' premises' to reach plaintiffs' ditch.'* (Emphasis supplied.)

As an additional ground for reversing the trial court the Supreme Court of Montana on the same page 673 of 105 P. 2d states:

“(15-17) *It is well settled that a subsequent appropriator attempting to justify his diversion has the burden of proving that it does not injure prior appropriators. Donich v. Johnson, 77 Mont. 229, 250 P. 963. Certainly here the defendants have not sustained that burden. It is apparent that they have not proved and cannot prove that their diversion would not in any case harm the plaintiffs simply by evidence as to the amount of flow of volume of water at defendants' dam or at a point a mile and a half below it. The only possible proof of such non-interference would be evidence, (1) that in spite of defendants' diversion there is actually available at the plaintiffs' point of diversion all the water for which they then have a beneficial use up to the limit of their appropriation; or (2) that if insufficient water is available there defendants' storage or diversion of water did not contribute to that result. Not only have the defendants failed to prove non-interference with plaintiffs' prior right, but the evidence shows affirmatively that there has been such interference and that it is still continuing.*

“*There is no question that one of the paramount needs of the semi-arid states is the conservation of water. However, it is not conserved by permitting a later appropriator utterly to destroy a prior appropriation for the irrigation of some 130 acres by an appropriation to irrigate approximately 30 acres.*”  
 \*\*\*” (Emphasis supplied.)

An early Idaho case (1904), *Moe et al v. Harger et al*, 10 Idaho 302, 77 Pac. 645, involved the same type of situation—injunction and defense that water if not diverted would not reach prior downstream appropriator. In its opinion upholding and affirming the trial court, which decided in favor of the prior appropriator and overruling the defense of the defendant, stated at page 647:

“\*\*\*Where prior appropriators have diverted the amount of water to which they are entitled, and, for example, say 100 inches, to which the next appropriator is entitled, is left in the stream, and a settler above diverts a part or all of the remaining water, the presumption must at once arise that such diversion will be to the injury and damage of the appropriator entitled thereto.

So soon as the prior appropriation and right of use is established, it is clear, as a proposition of law, that the claimant is entitled to have sufficient of the unappropriated waters flow down to his point of diversion to supply his right, and an injunction against interference therewith is proper protective relief to be granted. *The subsequent appropriator, who claims that such diversion will not injure the prior appropriator below him, should be required to establish that fact by clear and convincing evidence.*\*\*\*”

This case was cited with approval in *Silkey v. Tiegs*, (Idaho 1934) 28 P. 2 1037, 1038. And then too on page 646 of the Pacific Report is the following:

“\*\*\*This Court has uniformly adhered to the principle, announced both in the Constitution and by the statute, that the first appropriator has the first right; and it would take more than a theory, and in fact clear and convincing evidence, in any given case, showing that the prior appropriator would not be injured or affected by the diversion of a subsequent appropriator, before we would depart from a rule so just and equitable in its application, and so gen-

erally and uniformly applied by the courts. Theories neither create nor produce water, and when the volume of a stream is diverted, and 75 percent of it never returns to the stream, it is pretty clear that not exceeding 25 percent of it will ever reach the settler and appropriator down the stream, and below the point of diversion by the prior user.\*\*\*"

In the case just cited "experts" had theorized that water used by the upstream junior appropriator would not affect the amount of water available to the downstream prior appropriator. In the case now on appeal the "experts" theorized, in the face of concrete evidence to the contrary, that if Bagdad did not use the water above, it would not reach Zannaras-Robinson. The Idaho court's statement that "theories neither create nor produce water" is an apt expression.

The case of *Neil v. Hyde* (Idaho 1919) 186 Pac. 710, involved the burden of proof required when a junior appropriator claims that water used would not, if allowed to flow downstream, reach the prior appropriator. At page 713 on rehearing, the court stated:

"If neither the surface nor underflow, if undisturbed, would reach the point of diversion of the prior appropriator, his flow would not be diminished by the diversion of water above him by a junior appropriator, and he could not complain. *The burden rested upon appellants to show that neither the surface nor underflow, if uninterrupted, would reach the point of diversion of respondent, the senior appropriator.*"

The presumption in this case on appeal is that all water intercepted and diverted will decrease the flow of the creek. The office of this presumption is to give rise to the rule and cast the burden of proof under such circumstances, on the one intercepting and diverting the flow to show that such interception and diversion does not encroach upon prior appropriators.

In this case it is contended by Zannaras-Robinson that the District Court in its tentative order of January 3, 1951 (R. 10-12) and in the judgment of April 17, 1957 (32-35) based upon certain Findings of Fact and Conclusions of Law, conclusively shows that the Trial Court completely ignored, in the preliminary order, to take into consideration the fact that Zannaras-Robinson were the prior appropriators, and that, in the final judgment again not only failed to recognize the priority of Zannaras-Robinson but also failed to recognize the decision in Civil Cause No. 321, affirmed by this Appellate Court and mandated to the District Court, adjudicating the water rights of the parties.

As a result of such failure, the District Court then erroneously further failed to place the burden of proof upon Bagdad and to require Bagdad to prove by clear and convincing evidence that its admitted pumping operations and use did not interfere with the prior rights of Zannaras-Robinson. The judgment should therefore be reversed.

The judgment of January 2, 1951 was based upon erroneous findings of fact, resulted in an erroneous conclusion and erroneous judgment.

## RES JUDICATA

THIS ARGUMENT IS DIRECTED TO CONCISE STATEMENTS OF POINTS NUMBER 6, 8 and 18

“Briefly stated, the doctrine of res judicata is that an existing final judgment rendered upon the merits, without fraud or collusion, by a court of competent jurisdiction, is conclusive of rights, questions, and facts in issue, as to the parties and their privies, in all other actions in the same or any other judicial tribunal of concurrent jurisdiction.” 30 Am. Jur., Judgments, Sec. 161, page 908. See also 30 Am. Jur.,

Judgments, Secs. 165, pages 910-912, and Sec. 172, pages 914-917, and Sec. 179, pages 923, 924.

In support of the above citations from American Jurisprudence the following cases are cited:

The Haytian Republic (United States v. The Haytian Republic) 154 US 118, 38 L ed 930, 14 S Ct 992;

Dowell v. Applegate, 152 US 327, L ed 463, 14 S Ct 611;

Beloit v. Morgan, 7 Wall. (US) 619, 19 L ed 205;

Young v. Black, 7 Cranch (US) 565, 3 L ed 440;

Lawrence v. Vernon (CC) 3 Summ 20, Fed Cas No. 8, 146;

Hay v. Salisbury, 92 Fla. 446, 109 So 617, citing RCL;

Healy v. Moore, — Mo App —, 100 SW 2d, 601 citing RCL;

White v. Ladd, 41 Or 324, 68 P 739, 93 Am St Rep 732;

Howard v. Huron, 5 SD 539, 59 NW 833, 26 LRA 493;

Alderson v. Horse Creek Coal Land Co. 81 W Va 411, 94 SE 716, citing RCL.

Anno: 11 L ed 1059.

and the 1957 Cumulative Supplement adds to the above citations that of Ripley vs. Storer, 309 NY 506, 132 NE 2d 87, motion den 309 NY 976, 132 NE 2d 335.

Volume 50 C.J.S. Judgments, Section 682, page 128-133, contains a discussion of this principle.

Several hundred cases are cited in support thereof. So as not to burden the Court with all of these, however, the following Arizona cases are cited:

In re Sullivan's Estate, 51 Ariz. 483, 78 P 2d 132, 135;

Stewart vs. Phoenix Nat. Bk. 49 Ariz. 34, 64 P 2d 101;

Miller vs. Kearnes, 45 Ariz. 548, 46 P 2d 638, 640.

Another well reasoned case carrying out the above principles and also holding that the inquiry of *res judicata* is not limited to the mere formal judgment but extends to the pleadings, the verdict, or the findings, and that the scope and meaning of the judgment is often determined by the pleadings, verdict or findings, is:

Cressler vs. Brown et al (Okla. 1920) 192 P. 417.

It is also the contention of the Appellants that the matter of deprivation of water was passed upon and decided by the District Court (and affirmed by this Appellate Court) in Civil Cause No. 321 and cannot be relitigated in the present action. In support of this principle are the following cases:

Boland vs. Nihlros et ux (Utah 1932) 10 P 2d 930;  
Jeremy Fuel & Grain Co. vs. Mellen, 50 Utah 49,  
165 P. 791;

Price et al vs. Clement (Okla. 1940) 102 P 2d 595;

Sutphin vs. Speik (Calif. 1940) 99 P 2d 652;

Sutphin vs. Speik (Calif. 1940) 101 P 2d 497  
(Rehearing);

Yates vs. Kuhl (Calif. 1955) 279 P 2d 563;

Joyce vs. Murphy Land & Irrigation Co., Limited,  
et al (Idaho 1922) 208 P. 241;

Goodeagle vs. Moore 89 Okla. 211, 214 P. 725;

State ex rel Barnett, Bank Comr. vs. Wood, 171 Okla.  
341, 43 P 2d 136;

Bennett vs. City of Salem, 235 P. 2d 772;

Neil vs. Hyde et al. (Idaho 1919) 186 P. 710.

The case of Bennett vs. City of Salem (Oregon) *supra* contains a rather complete discussion of the matter of *res judicata*. Syllabus No. 5 thereto is:



“If second action involves a right, title or interest as to which the judgment on the first action is a conclusive adjudication, the estoppel must extend to every matter which might have been urged to sustain or defeat that right, title or interest even if the second action is different.”

On the basis of that case the judgment in Civil Cause No. 321 and its unanimous affirmance by this Appellate Court precluded the relitigation of the water rights of the parties hereto and the deprivation of water and the right of Zannaras-Robinson to take water from Burro Creek without interference by Bagdad. Further, the judgment in Civil Cause No. 321 acted as an estoppel as against all matters urged by Bagdad to defeat the rights of Zannaras-Robinson appearing on the record in Civil Cause No. 321, No. 14248 in this Court.

The same principle will be hereinafter discussed as applying also to the Rule of the Law of the Case.

It will be noted that the judgment dated November 12, 1953 (14248 R. 41-43) adjudged the validity and quieted the title of the water rights of the parties, holding that Zannaras-Robinson were the downstream prior and Bagdad the junior upstream appropriators, and as such senior appropriators Zannaras-Robinson were entitled to take water from Burro Creek without interference from Bagdad. The judgment was based on several findings, one of which was that for approximately five months in each year, due mainly to Bagdad's pumping operations and use of water above, there was no water at the Zannaras-Robinson point of diversion. (14248 R. 37-40)

Another question which arises is that of whether the Court could (after the entry of the judgment on Civil Cause No. 321 on November 12, 1953) hear Bagdad at the trial March 9-11, 1954 in its presentation of expert

testimony, based upon hypothetical assumptions, attempt to show that its pumping and use of the entire supply of the creek during the summer months was the use of water which would never reach the Zannaras-Robinson point of diversion.

It will be recalled that at the 1949 trial Bagdad claimed there was plenty of water in the creek for both diversions. At the 1952 trial Bagdad changed its position and claimed the lack of water at the Zannaras-Robinson point of diversion was due to natural causes. This 1952 trial was the consolidated trial of this cause of action and Civil Cause No. 321. Then at the 1954 trial Bagdad again changed its position and produced expert witnesses to attempt to prove by calculations based upon the hypothetical assumptions that when Bagdad pumps all the water out of the creek during the summer and a part of the fall months as the evidence and the Government water gauges show that it does, then this pumping and use will not affect the water downstream at the Zannaras-Robinson diversion point, because if the water was left in the stream it would have been lost by evaporation and evapo-transpiration before reaching the Zannaras-Robinson diversion point.

The judgment in Civil Cause No. 321 was appealed by Bagdad. During the pendency of the appeal, Zannaras-Robinson filed a motion for further hearing based upon the fact that Civil Cause No. 321 adjudicated and quieted the water priorities and rights of the parties, determined that Zannaras-Robinson were entitled to the use of water from Burro Creek without interference from Bagdad, and the judgment was based on the findings of fact that "For approximately five (5) months in each year, due mainly to plaintiff's (Bagdad's) pumping operation and use of water above, there was no water at the defendants' (Zannaras-Rob-

inson's) point of diversion." This motion was denied by minute entry November 23, 1953 (R. 644) "subject to renewal in the spring."

December 5, 1953 Zannaras-Robinson filed a Renewal of Motion to Set for Further Hearing and Affidavit in Support Thereof. Seven points were set forth as grounds for the granting of this motion. (R. 23-27).

Paraphrased they are:

That at the termination of the hearing the Court had announced that it desired evidence in order to determine the character of judgment to be entered in favor of Zannaras-Robinson;

That Zannaras-Robinson were under the impression that the Court had actually determined that they were entitled to a judgment and the character of judgment was the only matter to be determined;

That the decision of the Court in Civil Cause No. 321 (heretofore alluded to involving the same water rights, deprivation and parties) had been determined in favor of Zannaras-Robinson and was then on appeal to the United States Court of Appeals for the Ninth Circuit, but that the appeal did not operate as a stay of execution; that Zannaras-Robinson were entitled to a judgment in accordance with the evidence, enjoining Bagdad from using Zannaras-Robinson water;

That the evidence clearly showed that for five months each year Zannaras-Robinson were deprived of water by reason of Bagdad's pumping; and Zannaras-Robinson could not economically operate on an on and off basis;

That Zannaras-Robinson were desirous of immediately adding to their milling facilities involving the expenditure of some \$40,000, but that it was necessary to have assurance by the entry of a favorable decree in order that they would be assured of a continuous water supply;

That Zannaras-Robinson were negotiating with the owners of the Old Dick Mine for milling additional ore and that the contract would of necessity be of several years' duration and required sufficient water for running their mill continuously without interruption ;

That the decision in this case does not have to await the action of the Appellate Court on Civil Cause No. 321, then on appeal.

Without objection by Bagdad, this renewed motion to set cause for hearing was granted (R. 645), and hearing held March 9-11, 1954, which was at the time Civil Cause No. 321 was yet pending on appeal.

Instead of evidence being introduced by Bagdad for the purpose of determining at this hearing the character of judgment to be entered in accordance with the motion and the Court's decision in Civil Cause No. 321, the matter of the deprivation of water was relitigated. In the final analysis then we have in this judgment on appeal a judgment overruling in effect the Trial Court's opinion based on the same issues and facts. The judgment now being appealed was rendered April 17, 1957, after the former judgment's affirmance and final determination by this Appellate Court.

The effect of affirmance is discussed in 3 Am. Jur. Appeal and Error, Sec. 1166, page 677, 8 in part as follows :

"It may be stated generally that a judgment of affirmance is a determination by the appellate court that the proceeding under review is free from prejudicial error. Such action ends the case in the appellate court and deprives such court of all power to add to, or alter, the record as certified, by rescinding the order of affirmance and dismissing the appeal. All questions raised by the assignments of error and all questions that might have been so raised are to be regarded as finally adjudicated against the appel-

lant or plaintiff in error, and the judgment affirmed must be regarded as free from all error, even though errors were present which were not raised by the assignment of error and the record contains defects not discovered until after the judgment had been affirmed and the petition for rehearing denied.”

The principle that a fact or question which was actually and directly in issue in a former suit, and was there judicially passed upon and determined by a court of competent jurisdiction, is conclusively settled by the judgment therein, so far as concerns the parties to that action, and persons in privity with them, and cannot be again litigated in any future action between such parties or privies, in the same court, or in any other court of concurrent jurisdiction, upon the same or different cause of action is discussed in:

Price et al vs. Clement (Okla. 1940) 102 P 2d 595;

Goodeagle vs. Moore 89 Okla. 211, 214 P. 725;

United Tire & Inv. Co. vs. Hines, Okl. Sup. 96 P 2d 1047;

Morehouse vs. City of Everett (Wash. 1926) 252 P. 157;

Johnson vs. Gillett, 66 Okl. 308, 168 P. 1031;

Comanche Ice & Fuel Co. vs. Binder & Hillery, 70 Okl. 28, 172 P. 629;

Adams et al vs. State ex rel Mothersead Bank Com'r. 133 Okl. 194, 271 P. 946;

McKee, Ex'x. vs. Producers' & Refiners' Corp. et al 170 Okl. 559, 41 P 2d 466.

The Price et al vs. Clement case supra quotes with approval from syllabus 2 of State ex rel Barnett, Bank Com'r. vs. Wood, 171 Okl. 341, 43 P. 2d 136, as follows:

“When a fact has been determined in the course of a judicial proceeding and a final judgment has been rendered in accordance therewith, it cannot be again

litigated between the same parties without virtually impeaching the correctness of the former decision, which, from motives of public policy, the law does not permit to be done.\*\*\*”

In the instant case we have the judgment in Civil Cause No. 321 possessing the following characteristics:

Final judgment

Rendered without fraud or collusion

Rendered on the merits

Rendered by a court of competent jurisdiction, in fact the same court

Rendered between the same parties

Involving the same water rights

Involving deprivation of water

being the issues in the instant case, and having been finally adjudicated (and affirmed by this Appellate Court) in Civil Cause No. 321, the matter is now *Res Judicata*, and was *Res Judicata* at the time of the entry of the judgment on April 17, 1957.

This Argument is urged in support of Concise Statements of Points Number 8, 1 and 15.

## AFFIRMANCE BY APPELLATE COURT LAW OF THE CASE

The doctrine of the law of the case clearly applies to questions of law actually presented and determined upon a former appeal or error proceeding as essential to its just disposition. Likewise, matters necessarily involved in the determination of a question are settled by the decision when the same are again presented on a subsequent appeal. So, the decision upon a prior appeal is conclusive where the conclusion declared could not have been reached without either expressly or impliedly deciding such questions. 3 Am. Jur. Appeal and Error, Sec. 994, page 549.

The general rule, supported by the great weight of authority, is to the effect that questions which might have been, but were not, raised or presented on a prior appeal, or error proceeding, will not be considered on a subsequent appeal, or error proceeding—in other words, that where the prior judgment was on the merits, nothing is before the court on a subsequent appeal except the proceedings subsequent to the first mandate, all matters occurring prior thereto and which could have been adjudicated on the former hearing being regarded as controlled by the law of the case rule. 3 Am. Jur. Appeal and Error, Sec. 995, page 549.

It may be stated generally that a court of review is precluded from agitating questions which were propounded, considered and decided on a previous review. The decisions agree that as a general rule, when an appellate court passes upon a question, the question there settled becomes the “law of the case” upon a subsequent appeal. 3 Am. Jur., Appeal and Error, Sec. 985.

When the reviewing court, upon the consideration of the first appeal, leaves none of the points and issues disposed of to be retried after the mandate, there is of course an added reason for considering all decisions (including findings and conclusions) on the first appeal as constituting the Law of the Case, and therefore conclusive upon the second appeal. 3 Am. Jur. Appeal and Error, Sec. 985.

The Law of the Case is applicable to separate cases involving the same facts and issues which have been previously determined on appeal.

The point of application of the Law of the Case to a decision in another case and not only to the subsequent appeal of the same case is discussed in 5 C.J.S. Appeal and Error, Section 1964, page 1499, 1501. It cites in

support of the proposition, *Tally vs. Ganahl* 151 Cal. 418, 90 P. 1049.

Other cases recognizing that the Law of the Case may be applied to separate and distinct cases are:

*Portland Trust Co. vs. Coulter*, 23 Or. 131, 31 Pac. 280;

*Hawley vs. Smith*, 45 Ind. 183;

*Wilkes vs. Davies*, 8 Wash. 112, 35 Pac. 611, 23 L.R.A. 103;

*Norwood vs. Eastern Oregon Land Co.* (Oregon 1931) 5 P. 2d 1057;

*Wilkes vs. Davies*, (Wash. 1894) 35 P. 611;

*Farmers' State Bank & Clayton Nat. Bk.* (New Mexico 1925) 245 P. 543.

In the case of *Portland Trust Co. et al vs. Coulter et al supra*, after determining that the Law of the Case was applicable to a separate case, the Court then discussed an argument advanced that in spite of invoking the Rule of the Case, the judgment should be different in the case then on appeal. In discussing this point, the Court said at Page 281 of the Pacific Report:

“If this was an open question on this appeal, in view of counsel’s argument, we might feel induced to carefully re-examine the question, *but the law is well settled that a decision of this court upon a point distinctly made becomes in all subsequent proceedings between the same parties, concerning the same subject-matter, and upon the same facts, the law of the case by which we are bound*, whatever our views might be upon an original consideration of the matter. Wells, Res Adj. c 44. ‘A previous ruling by the appellate court upon a point distinctly made,’ says Mr. Chief Justice FIELD, ‘may be only authority in other cases, to be followed and affirmed, or to be modified or overruled, according to its intrinsic merits, but, in the case in which it is made, it is more



than authority; it is a final adjudication, from the consequences of which the court cannot depart, nor the parties relieve themselves.' *Phelan v. San Francisco*, 20 Cal. 39." (Emphasis supplied)

This case also quotes with approval from *Stacy Railroad Co.* 32 Vt. 552, where the question, "will this court revise a former decision made by the same court in the same cause, and on substantially the same state of facts" by stating that to ignore the former decision and change it when appealed again "would lead to incalculable mischief." It then continues with the statement that, "If all questions that have ever been determined by this court are to be regarded as still open for discussion and revision in the same cause, there would be no end to their litigation, until the abilities of the parties or the ingenuity of their counsel was exhausted."

This same *Portland Trust Co.* case *supra* also cites with approval from *Bridge Co. vs. Stewart*, 3 How. 413, and points out at Page 281 of the *Pacific Report* that:

"\*\*\*Although the question (involved in *Bridge vs. Stewart*) was the important one of jurisdiction, it was, notwithstanding, held that the former decision of the Court in the same case was conclusive of the rights of the parties, and could not be reconsidered upon a second appeal; such an appeal bringing under review only the proceedings of the circuit court subsequent to the mandate." (Bracketed words within quote supplied);

and cites the following cases as being to the same effect:

*Davidson vs. Dallas*, 15 Cal. 75;  
*Kibler vs. Bridges*, 5 S. C. 335;  
*Huffman vs. State*, 30 Ala. 532;  
*Hawley vs. Smith*, 45 Ind. 183;  
*Parker vs. Pomeroy*, 2 Wis. 84;  
*Page vs. Fowler*, 37 Cal. 100;  
*Thomson vs. Albert*, 15 Md. 268.

In this same Portland Trust Co. case *supra*, the Court continues at Page 282 of the Pacific Report with:

“It is the points distinctly presented and decided which become the law of the case, and the reasons or want of reasons for the decision are of no consequence on this appeal. The effect of the decision in *Coulter v. Portland Trust Co.* is that the deed from Mrs. Palmer, as attorney in fact for her husband, to W. G. Jenne is void, and did not convey the title, and we have no alternative but to assume that all the reasons urged for a contrary conclusion were duly considered by the court, and adhere to that decision on this appeal.”

Vol. 3 Am. Jur. Appeal and Error, Section 531, page 194, discusses the divestiture of jurisdiction of the District Court over the subject matter being appealed. The first sentence is:

“An appeal or error proceeding divests the trial court of jurisdiction over matters necessarily involved in the review proceeding only.”

(Citing *White vs. White*, 106 Pa. Super. Ct. 85, 161 A. 464)

Vol. 3 Am. Jur. Appeal and Error, Section 1234, page 730, 731 discusses the duty of the trial court to comply with the mandate of the appellate court. In part the discussion is:

“After a case has been determined by the reviewing court and remanded to the trial court, the duty of the latter is to comply with the mandate of the former. The mandate of the reviewing court is binding on the lower court and must be strictly followed and carried into effect according to its true intent and meaning, as determined by the directions given by such reviewing court. Public interest requires that litigation shall come to an end speedily, so that when a cause has been tried to judgment, and the merits

of the trial determined upon appeal, the trial court upon remittitur, has no power but to obey the judgment of the appellate court. It may, by various methods, be compelled to comply with that mandate; and if it misconstrues the direction of the reviewing court, does not give full effect to its mandate, or enters a judgment or decree which is not in conformity thereto, a new review is appropriate. Proceedings contrary to the mandate must be treated as null and void.\*\*\*''

Applying the principle of the Law of the Case to this case on appeal, we find that the question of the rights of the parties, including the priority right of Zannaras-Robinson to take water from Burro Creek without interference by Bagdad and deprivation of water by Bagdad, were expressly presented to this Court in Civil Cause No. 321, and affirmed by this Appellate Court in Appeal No. 14248, reported in 229 F 2d 920.

The points relied upon by Bagdad in its appeal are set forth in 14248 R. 433-436.

It will be seen that the very issues on this appeal, i.e. rights and priorities of the parties, including the priority right of Zannaras-Robinson to take water from Burro Creek without interference by Bagdad, and deprivation of water by Bagdad were previously expressly before this Appellate Court. In addition, these issues were argued in the briefs on that appeal and a final judgment on these issues rendered, and then unanimously affirmed by this Appellate Court. As a matter of fact, the Complaint filed by Bagdad in Civil Cause No. 321 was by reference incorporated in and made a part of Bagdad's Answer to the Zannaras-Robinson Amended Petition for Relief, and Bagdad prayed for the same relief in this case as it sought in Civil Cause No. 321. (R. 22, 23)

In addition, at the commencement of the consolidated trial of Civil Causes No. 221 and 321 on May 13, 1952, the Court said: (14248 R. 52)

“The Court: Why not consolidate? It is all the same issue.”

Also, Bagdad in its reply brief (P. 3) in this Court in the appeal of Civil Cause No. 321 (14248 on appeal) argued that Cause No. 321 was brought in an attempt to defeat Civil Cause 221, this cause now on appeal.

By invoking the rule of the Law of the Case on this appeal, the District Court was bound by the mandate of this Appellate Court, which mandate is dated March 2, 1956. Under the rule of the Law of the Case the District Court was bound to follow that mandate and was precluded from considering any matter occurring prior to the date of the mandate.

By the terms of the judgment here on appeal the District Court nullified, impeached, reversed and overruled the former judgment and misconstrued and failed to carry out the mandate of this Appellate Court.

A fortiori the Law of the Case being applicable herein the decision of April 17, 1957 must be reversed and there is no necessity for even considering all of the additional points of error.

This argument is urged in support of Concise Statement of Points Number 2, 3, 4, 5, 8, 9, 10, 11, 12, 14 and 18.

### PRIMA FACIE CASE

In the Zannaras-Robinson Renewal of Motion to set for further hearing filed December 5, 1953, the adjudication in Civil Cause No. 321 was pled. Without objection from Bagdad the matter was set. At that time the Court had before it the evidence theretofore taken on

March 3 and 4, 1949 (R. 38-346), and the evidence theretofore taken on May 13 and 14, 1952 (14248 R. 51-368). Additional evidence was then taken March 9 and 10, 1954. (R. 347-636). This latter evidence was taken at a time subsequent to the entry of the findings of fact, conclusions of law and judgment of the United States District Court for the District of Arizona in Civil Cause No. 321, dated November 12, 1953 (14248 R. 37-43), which judgment was then on appeal to this Court, being assigned by this Court Cause Number 14248. The judgment was affirmed by this Appellate Court on January 30, 1956, 229 F 2d 920.

For the purpose of the further hearing on March 9 and 10, 1954, proceedings were based on the fact that Zannaras-Robinson had a valid decreed water right. The attorney for Bagdad at the commencement of and before any witnesses were heard said:

“In that connection, I want to briefly call your Honor’s attention to this: If we assume that Mr. Zannaras has a valid water right, which, for the purpose of this proceeding, we must, his water right is for 3 million gallons per year.” (R. 352)

Therefore it was distinctly understood and admitted at the 1954 hearing that there was a judicially decreed right in Zannaras-Robinson for the use of water from Burro Creek.

In addition, the judgment in Civil Cause No. 321 (Appeal No. 14248) decreed that Zannaras-Robinson were entitled as prior appropriators to take water from Burro Creek without interference from Bagdad. Such judgment was based upon several findings of fact, among them being the finding that for approximately five months each year, due mainly to Bagdad’s pumping operations and use of water above, there was no water at the Zannaras-Robinson point of diversion.

The finding and judgment was based upon evidence taken at the consolidated trial of this case and Civil Cause No. 321. It was not only before the same Judge in the same Court, but the evidence was taken at the same hearing.

Zannaras-Robinson presented their Certificate of Water Right and put on evidence showing the lack of water at their point of diversion, showed no other speedy and adequate remedy at law. Bagdad in its pleadings and all of its evidence admitted it was pumping water the year around from Burro Creek and that in the summer months it was pumping all the available water from Burro Creek. At this point Zannaras-Robinson had established a *prima facie* case. Having established a *prima facie* case, the burden was upon Bagdad to show by clear and satisfactory evidence that its admitted excessive pumping and use of water did not affect the flow of water at the Zannaras-Robinson point of diversion.

The effect of the failure of Bagdad to establish an affirmative defense by clear and satisfactory evidence has been covered in the argument entitled *Burden of Proof*. In order that we will not unnecessarily burden the Court we are content to only point out a few citations.

*Medano Ditch Co. v. Adams*, 29 Colo. 317, 68 Pac. 431, 435.

*Kinney on Irrigation and Water Rights*, Second Edition, Section 1628, Vol. 3, page 2974, sets forth very succinctly the matter of making a *prima facie* case when the priority has been judicially decreed.

Additional citations on this point are set forth in the *Argument on the Burden of Proof*.

Bagdad did not, until the 1954 hearing, ever urge in the record that water would not reach the Zannaras-Robinson point of diversion if Bagdad would not pump and use any water during the summer months. Irrespective of this fact, we find that in Bagdad's reply brief (P. 6) in the former appeal of No. 14248, filed with this Appellate Court in July of 1954, (after the March 1954 hearing on this case by the District Court), that the Albion-Idaho Land Co. vs. NAF Irr. Co., 97 F 2d 439 was urged upon this Appellate Court as grounds for reversing that judgment, which judgment was based on the same facts and issues involved in this case on appeal and, in fact, evidence adduced at the consolidated trial. By the affirmance of that case the application of the principle was found inapplicable to the controversy between these parties. In spite of this the Trial Court based the judgment in the present case on a case this Appellate Court had already rejected as authority.

While we feel that we have disposed of the Albion-Idaho case *supra*, it should be pointed out that there are other reasons that it is not analogous to the present case.

The Albion-Idaho case *supra* was an injunctive action by lower appropriators against upper appropriators, both of whom claimed to be prior appropriators. They were residents of different states. The lower appropriators sought the appointment of a water master to administer the waters. Certain decrees adjudicating water rights, to which decrees the present parties were not parties, and a decree whereby a court in one state purportedly adjudicated rights in another state, were set up as the basis for establishing adjudicated rights. The matter was heard by the trial court and it concluded that the evidence was not sufficient for it to

determine whether water would reach the lower appropriator even if not used by the upper appropriator. The judge thereupon, with the consent of the parties, appointed a water master, who put on gauges and checked the flow of the stream for more than three years and then made a report to the Court. A very elaborate injunction was then granted, setting limits upon the times when the upper users must let the water down according to the water gauges, and established a formula for determining the times when the upper appropriators need not let water down, predicated on the fact found by the Court that the water if let down the creek would not reach the lower appropriators during certain times. This fact was based on actual accurate measurements of water gauges installed by the Commissioners.

The case went to the Appellate Court on a statement of the evidence, with the record not containing the evidence in full. Of course when the Appellate Court does not have the entire record before it such appellate court will presume any conceivable state of facts within the scope of the pleadings and not inconsistent with the record which will sustain the decision below. The Appellate Court so ruled.

So far as the decrees were concerned, since the present parties were not parties or privies to the parties to those decrees, the decrees were not binding on the present parties. And the decree purporting to Adjudicate water rights in another state was beyond the Court's jurisdiction. The Appellate Court so ruled.

The main point at issue after determining from the agreed statement of the evidence and the facts obtained by the Commissioners appointed with the consent of both parties, was when and how much water should be



let down by the upper junior appropriator in order that water so released would be available for the lower appropriator's use.

It is to be noted that the burden of proof was not involved in the Albion-Idaho case. It was submitted on a statement of evidence and the entire evidentiary record was not before the Appellate Court.

It was not an adjudication case (as it had no jurisdiction to adjudicate priorities), and there was no former decree. We have in the case now on appeal a case between the same parties, covering the same issues of rights of the parties, including the decreed right of Zannaras-Robinson to use water from Burro Creek without interference by Bagdad and the deprivation of water by Bagdad. This Appellate Court affirmed that judgment in Cause No. 14248.

In this case on appeal, Zannaras-Robinson having presented to the Trial Court a prima facie case, and Bagdad having failed to carry the burden of proof, (not only as shown by the evidence but as shown by the Court's Memorandum, Findings of Fact and Conclusion), as to its admitted pumping and use of water not interfering with Zannaras-Robinson's prior rights, the Trial Court should have granted the injunction.

This Argument is urged in support of Concise Statement of Point No. 16.

## CHANGE OF METHOD AND MEANS OF DIVERSION

The Certificate of Water Right obtained by Bagdad from the State Land Commissioner of the State of Arizona was introduced in evidence both in the 1949 trial and in the consolidated trial in 1952. It is Ex. L-1 of the 1949 trial and is Ex. J of the 1952 trial. (14248 R. 397-400)

The Certificate of Water Right contains the following condition: (14248 R. 399)

"The right to the use of water aforesaid hereby confirmed is restricted to the lands or place of use herein described, and subject to all prior existing rights."

It is the contention of Zannaras-Robinson that the certificate precluded Bagdad from changing its method and means of diversion, which change resulted in depriving Zannaras-Robinson of Water which formerly returned to the stream and also increased the quantity of Bagdad's use. It is also contended that the burden is upon the appropriator changing the method and means of use to show that such change does not damage another appropriator, whether he be a prior or subsequent appropriator.

The Bagdad Certificate of Water Right heretofore referred to was issued by the State of Arizona April 12, 1944. Mr. Dickie became manager of Bagdad in September 1944 (R. 172)

On direct examination Mr. Dickie testified as follows: (R. 172-175)

"Q. After you came to the Bagdad in September, 1944, Mr. Dickey, I think you rearranged the disposal of tailings, is that correct? A. Yes, sir.

"Q. And likewise, rearranged to some extent the method of securing water for mining, is that right?

"A. Well, you might state it that way, if I may be allowed to explain. The prior management, in designing the plant and the disposal of tailings, installed a large seven-inch trestle line three and one-half miles downstream and ran the tailings from the mill to that point and stored them on the bank of Boulder Creek. It was a costly operation to keep the pipeline maintained, to keep it from breaking down, also there wasn't a chance of reclaiming any water. At that time we was interested in reclaiming all the mill

water possible, because there wasn't any saving in re-agents at the same time other than in having to pump water from Burro Creek seven and one-half miles. Therefore, we began construction of a tailings pond right at the millsite within twelve or fifteen hundred feet, and from that date on we have continued to store our tailings right at the property at the millsite."

\* \* \*

And continued:

"Q. In placing of that dam across Moroney Gulch, you call it? A. Yes.

"Q. Approximately what amount of material was moved in there? A. Two million yards.

"Q...And it was approximately that time when you started to make this change that you heard from Mr. Zannaras? Is that right? A. Yes.

\* \* \*

"Q. The way you have that arrangement there, I believe, Mr. Dickey, the tailings now are run directly from the mill and are dammed behind this dam?

"A. Yes, sir.

"Q. What do you then use the water for?

"A. We use the water over and over in the mill for our milling operations.

"Q. You mean that the tailings are such that you can pump water back out and use it in your mill there?

"A. As the tailings go into the dam, they go in there with approximately 30 per cent solids, the balance being water, and after it sets in the pond awhile, the tailings settle and it leaves clear water for us to use over again.

"Q. In other words, you keep circulating your water which is supplemented by fresh water from Burro Creek, is that right? A. Correct, sir."

This circumstance was argued in Appellates' opening brief (P. 9) in Appeal Cause No. 14248.

From Mr. Dickie's testimony the following indisputable facts appear to be true:

After September first 1944 and after the issuance of the Bagdad Certificate of Water Right (being dated April 12, 1944 Ex. J 14248 R. 397), Mr. Dickie rearranged the method of securing water for mining purposes, thereby reclaiming water which previously returned to Boulder Creek and hence to Burro Creek, below Bagdad's point of diversion and above the Zannaras-Robinson point of diversion downstream, both on Burro Creek.

Mr. Dickie gave accurate figures of the amount of water that was returning to the creek. He said that Bagdad was milling 3,000 tons of ore per day, (R. 171) prior to the time the change was made, and that in order to have the tailings flow the  $3\frac{1}{2}$  miles downstream to the bank of Boulder Creek, Bagdad had to put water in with the finely ground tailings to make it contain 30% solids and 70% water (R. 175).

Multiplying 7,000 tons of water put in the tailings daily by 365 days a year we find that this amounts to 2,550,000 tons of water which was returning to the creek, and since there are 240 gallons of water per ton, the amount of water returning to the creek amounted to 612,000,000 gallons of water. However, since about 3% of the ore was retained as copper concentrates, the amount of water reclaimed by Bagdad under the changed condition will amount to approximately 500,000,000 gallons of water now being reclaimed which is not, as formerly, returned to the stream.

The fact that Bagdad originally pumped out of Burro Creek a large amount of water and then later by changing its method of use stopped its return to the creek is shown in the record from the cross-examination of

Mr. C. H. W. Smith, Engineer for the Arizona State Land Department: (R. 325, 326)

“Mr. Cox: I will ask you if, under date of March 15th, 1944, the Bagdad Corporation gave a notice of complete application of water to beneficial uses, showing 600,000,000 — using 600,000,000 gallons of water per annum?

“Mr. Wilmer: I object to that as being immaterial, since that was in '44. We are here concerned with '48.

“Mr. Cox: Mr. Dickey testified there has been no material change in the amount of - - -

“Mr. Wilmer: Mr. Dickey didn't testify to any such thing at all. They put in their tailing pond since then.

“Mr. Cox: They had some pumps since then, but he said they had some pumps - - -

“Mr. Wilmer: I object on the ground it is immaterial what might appear in the proof of appropriation in 1944.

“The Court: It may be received.

“Mr. Cox: There was that record furnished to your office by the Bagdad Corporation, was there not?

“A. Yes.”

It is therefore established by this testimony that Bagdad filed a proof of appropriation, a statement under oath, that Bagdad pumped from Burro Creek 600,000,000 gallons of water prior to March 15, 1944. Of this amount pumped, approximately 500,000,000 gallons each year was returned with the tailings to the creek.

At that time Bagdad had a pump on Burro Creek with a rated capacity of 750 gallons per minute or a rated yearly capacity of 394,200,000 gallons of water, besides the other point of diversion on Boulder Creek as shown on Bagdad's Certificate of Water Right (14248 R. 397), that is, that they had the capacity to

do so in 1944 when Bagdad filed its proof of appropriation for 600,000,000 gallons of water. According to the testimony of Mr. Dickey as to the procedure, about 500,000,000 gallons of water was returning to the stream. As a result, the water at the Zannaras-Robinson point of diversion was polluted from 1943 up until the time the change was made. The pollution proves that the water returned to the creek by Bagdad reached the Zannaras-Robinson point and is substantiated by the judgment rendered in Civil Cause No. 129. The judgment awarded Zannaras-Robinson of \$1,000 for damages for such pollution and enjoined continued pollution. (14248 R. 431, 432)

Ex. 13 (14248 R. 369, 370) sets forth in letter form an exchange of correspondence between the parties looking toward the entry of judgment in Civil Cause No. 129. The result of this change in method of diversion resulted in removing the pollution and *at the same time drying up the creek.*

It should be noted that when Bagdad objected to the introduction of evidence as to the conditions existing at the time of the issuance of the Certificate of Water Right in 1944, stating, “\*\*\* that was in '44. We are here concerned with '48” (R. 326) Bagdad thereby ignored the fact that these conditions were material issues in cases when changes in method of diversion **take** place after the issuance of a Certificate of Water Right, in that such changes are prohibited when they will interfere with existing rights or increase the use of water. The Court recognized this when this evidence of the Engineer for the State was admitted over Bagdad's objection.

Where it is claimed that the change in method of diversion does not increase the amount of use, the burden of proof is upon the one who changes the method

of diversion and use to show that such change will not interfere with vested rights.

In this case now on appeal, evidence by Bagdad admitted the change in method of diversion and use. It then set forth in detail that the purpose of the change was so that the water could be reclaimed and used and reused. It then devolved upon Bagdad to establish that such change would not interfere with vested existing rights.

The following cases are urged in support thereof:

Mannix & Wilson et al vs. Thrasher, et al. (Mont. 1933) 26 P 2d 373;

Gassert vs. Noyes et al. 18 Mont. 216, 44 P. 958;

Farmers Highline Canal & Reservoir Co. et al. vs. City of Golden et al. (Colo. 1954) 272 P 2d 629;

Enlarged Southside Irrigation Ditch Co. vs. John's Flood Ditch Co. 116 Colo. 580, 183 P 2d 552;

Van Tassel Real Estate & Live Stock Co. vs. City of Cheyenne et al. (Wyo. 1936) 54 P. 2d 906;

Tudor vs. Jaca et al. (Ore. 1946) 165 P 2d 770.

The cases cited above also consistently hold that any change in method of diversion and use which injures other appropriators is prohibited, without making a new application therefor. Such application for additional appropriation being subject to other rights existing at that time.

If for no other reason than that the evidence conclusively showed the increased use by change in method of diversion and use, the Trial Court erred in not granting the injunction to Zannaras-Robinson.

This Argument is urged in support of Concise Statement of Point No. 20.

## ADMITTED USE OF MORE WATER THAN ENTITLED TO USE UNDER CERTIFICATE OF WATER RIGHT

Exhibit J. (14248 R. 397) is the Bagdad Certificate of Water Right dated April 12, 1944, fixing the priority date of November 5, 1941, stating in part that Bagdad's use is limited as follows: (14248 R. 398)

“\*\*\*is limited to an amount actually beneficially used for said purposes, and shall not exceed Three Hundred Fifteen Million Three Hundred Sixty Thousand (315,360,000) Gallons Per Annum.”

The principle that an appropriator may not use water in excess of the amount of his certificated right applies to all appropriators, irrespective of their priority.

This is forcefully brought out even as regards a prior appropriator in the following:

Kinney on Irrigation and Water Rights, Second Edition, Vol. 2, Sec. 784, page 1366, citing:

Tudor vs. Jaca et al. (Ore. 1946) 165 P 2d 770.

To the same effect is:

Farmer's Highline Canal & Reservoir Co. et al vs. City of Golden et al. (Colo. 1954) 272 P 2d 629.

At the 1954 trial Dr. Heinrich Theil testified that Bagdad in the year 1953 took from the stream 1,100 acre feet of water. (R. 471) This amounts to 358,436,100 gallons of water. This is contrasted to Bagdad's Certificate of Water Right to the effect that its use shall not exceed 315,360,000 gallons per annum. The same capacity pump was used from 1943 through 1953. (R. 577)

On the basis of the admitted use by Bagdad of water to the extent of some 43,076,000 gallons per annum in excess of the amount allowed by its water right cer-



tificate, the Trial Court erred in not granting to Zannaras-Robinson the injunctive relief for which they prayed.

This Argument is urged in support of Concise Statement of Point No. 17.

## USE OF WATER FOR PURPOSES OTHER THAN ITS OWN MINING OPERATIONS

Exhibit J of the 1952 trial is the same as Exhibit L-1 of the 1949 trial. (14248 R. 397-400) It is the Certificate of Water Right issued to Bagdad by the State of Arizona. The certificate contained therein a limitation as follows: (Ex. J, 14248 R. 398)

“\*\*\*that the amount of water to which such right is entitled and hereby confirmed, for the purposes aforesaid, is limited to an amount actually beneficially used\*\*\*”

Then follows a description of the lands owned by Bagdad.

At the 1949 trial cross-examination of Mr. Ernest R. Dickey, elicited the following: (R. 221, 222)

“Q. I believe you stated yesterday that you were using around 100,000 gallons per day for domestic purposes? A. Yes, sir.

“Q. Now, is that for the Bagdad employees?

“A. Anyone that lives there; everyone.

“Q. And there are other mining camps, miners from other mining camps also living at Bagdad?

“A. Yes, sir.

“Q. Hillside miners live at Bagdad? “A. Yes, sir.

“Q. Is there any charge made to the Hillside mine or to the miners for the water? A. No, sir.

“Q. Is the Hillside Mine a part of the Bagdad operations? A. No, sir.

“Q. The water is used for landscaping and gardening also at Bagdad? A. Yes, sir.

“Q. I believe you stated that they had—that you used approximately four to five thousand gallons per day of fresh water in your milling?

“A. Yes, sir.

“Q. Now, in your domestic water do you include the gardens in your computation of that?

“A. Yes.

“Q. Are there any other mining claims or mines that there are miners also living at Bagdad and you furnish water to? A. Yes, sir.

“Q. Which others?

“A. Goodwin’s Mining Company No. 2 Mines.

“Q. Are those near there? A. Yes, sir.

And further: (R. 226)

“Q. Is there any water taken from Bagdad to the Goodwin property? A. Yes.

“Q. How much water is taken over there?

“A. I have no idea.

“Q. What is it taken over there for?

“A. Drilling purposes, mining purposes and cooling engines, and so forth.

“Q. In other words, the Bagdad, the water that they are using from Burro Creek is also being used for the Goodwin property in the development there?

“A. Correct.”

This evidence clearly proves by Bagdad’s own evidence that Bagdad is using water in violation of its Certificate of Water Right by passing on a portion of water which it is taking from Burro Creek to other mining companies.

A right of appropriation does not carry with it any right to sell or give it to others, thereby depriving a prior appropriator (even subsequent appropriators) of their right to use the same. *Creek vs. Bozeman Waterworks Co.* 15 Mont. 121, 38 P. 459.

To the same effect:

*Hague vs. Nephi Irr. Co.* 16 Utah 421, 52 P. 765;

*Manning et al. vs. Fife et al.* 17 Utah 232, 54 P. 111;

*Enlarged Southside Irrigation Ditch Co. vs. John's Flood Ditch Co.* 116 Colo. 580, 183 P 2d 552;

*Farmers Highline Canal & R. Co. vs. City of Golden* (Colo. 1954) 272 P. 2d 629.

It is evident that Bagdad is not only pumping approximately 43,076,000 gallons more than the limit of its Certificate of Water Right but that in addition it is selling or giving away water to other mining companies, mining camps and others, also contrary to law.

This is an action in equity, requiring equitable relief. The Trial Court in refusing to grant injunctive relief by enjoining Bagdad, in fact encourages Bagdad to continue its illegal activities, at the expense of vested rights of prior appropriators. The Trial Court erred in failing to grant the injunction as prayed by *Zanaras-Robinson*.

This Argument is urged in support of Concise Statements of Points No. 1, 8 and 15.

FINDINGS OF THE STATE ENGINEER ARE ENTITLED TO GREAT RESPECT AS REPRESENTING THE OPINION OF AN EXPERT UPON A MATTER WITHIN THE RANGE OF HIS SPECIAL KNOWLEDGE AND EXPERIENCE

The State Land Department in the State of Arizona is specifically given control and supervision of the

waters of the state and investigative powers, Arizona Revised Statutes, Sections 45-102 and 103.

At the 1952 consolidated trial of this cause and Civil Cause No. 321, Mr. C. H. W. Smith, the Engineer for the Water Department of the Arizona State Land Department, testified. (14248 R. 110) He stated that he had made an official investigation, in person, of the conditions at the Zannaras-Robinson point of diversion November 9, 1949 (14248 R. 110), and again on November 14, 1950 (14248 R. 116).

His direct and cross-examination cover pages 14248 R. 110-120. Briefly, he testified that on both of these occasions there was no water flowing at the Zannaras-Robinson diversion point, that the creek was dry with the exception of small pot holes, and that there was no water which could be pumped by Zannaras-Robinson at their point of diversion.

The Trial Court's Finding of Fact No. 2 is: (R. 33)

"2. Burro Creek is a seasonal stream, generally wasting away, or tending to waste away, during the months of June, July, August, and on occasion, September in each year, depending upon the rainfall on it (sic) watershed. During the remaining months of the year there is generally adequate water in Burro Creek for all claims of both plaintiffs and defendant."

Such a finding is in direct conflict with the official finding of Mr. C. H. W. Smith, the Engineer for the Arizona State Land Department, who testified that he went to the Zannaras-Robinson point of diversion on November 19, 1949 and November 14, 1950, and that there was no water there on either occasion.

Great respect should be given to an official finding of a state engineer as representing the opinion of an expert upon a matter within the range of his special

knowledge. This principle is discussed, followed and the trial court's judgment reversed because of the trial court's failure to accord credence to a state engineer's official report in the following case:

In re Bassett Creek and its Tributaries in White Pine County, (Nev. 1945) 155 P 2d 324, citing as authority Barber Creek, 43 Nev. 403, 182 P. 925;

Scossa vs. Church, 46 Nev. 254, 205 P. 518, 210 P. 563; Deepwater Railway Co. vs. Honaker et al, 66 W. Va. 136, 66 SE 104, 27 L.R.A., N.S., 388, at p. 394.

To the same effect:

Smyth vs. Jenkins, (Ore. 1956) 299 P 2d 819.

Furthermore, at the same consolidated 1952 trial of this case and Civil Cause No. 321, Mr. Sherman O. Decker, Engineer in Charge, U. S. Geological Survey, Surface Water Division, testified. (14248 R. 128-130)

He testified that he went to the Zannaras-Robinson diversion point November 23, 1950 in his official capacity to locate a gauging site and to see what the flow conditions were. (14248 R. 129) He testified that there was no flow in the creek at the Zannaras-Robinson diversion point. (14248 R. 129) He also testified that plaintiffs' Ex. 5 consisting of 3 pictures showing the dry creek bed at the Zannaras-Robinson diversion point were taken while he was there. (14248 R. 129)

Evidently no consideration whatsoever was given to the testimony of this Engineer for the Surface Water Division of the U. S. Geological Survey as Finding of Fact No. 2 is in direct conflict with this definite testimony.

On the other hand, the testimony of both Mr. C. H. W. Smith, Engineer for the State Land Department and that of Mr. Sherman O. Decker, Engineer in Charge of the Surface Water Division of the U. S. Geological

Survey is in complete agreement with Finding of Fact No. III of the Judgment rendered by the same judge on the same evidence in Civil Cause No. 321, affirmed by this Appellate Court in No. 14248. (14248 R. 39) It will be recalled that the finding was that, “\*\*\*For approximately five (5) months in each year, due mainly to plaintiff’s (Bagdad’s) pumping operations and use of water above, there was no water at the defendants’ (Zannaras-Robinson) point of diversion.” (Bracketed words within quote supplied (14248 R. 39).

The Court’s finding being in direct conflict with the official finding of the water engineers, it follows that the Court’s finding is in error. Therefore the judgment must be reversed.

This Argument is urged in support of Concise Statement of Point No. 13.

### THE JUDGMENT IS CONTRARY TO THE WEIGHT OF THE EVIDENCE

It is the position of Zannaras-Robinson that the preliminary order, denying an injunction and retaining jurisdiction for the purpose of the entry of further orders should justice and equity so require, is contrary to the weight of the evidence and that the final judgment denying injunctive relief is contrary to the weight of the evidence.

The first trial was held March 3rd and 4th 1949. At this trial the evidence of Zannaras-Robinson was that there was insufficient water in Burro Creek during certain portions of the year, due to the pumping and use by Bagdad above, for Zannaras-Robinson to carry on mining and milling activities. Bagdad’s defense was that although it was pumping and using large amounts of water, there was plenty of water in the stream for Zannaras-Robinson at all times. It produced witnesses

A. D. Lon Adams, George H. Davis, Ernest R. Dickey, Ernest George Green and C. S. Staggs, all of whom testified as to there being lots of water in Burro Creek throughout the entire year, and in the summer months in particular. All of the Zannaras-Robinson witnesses, John P. Robinson, Jr., Arthur J. Seeds, C. A. Thompson and John Phillip Zannaras testified that there was no water at the Zannaras-Robinson diversion point during certain periods of the year, and that because of the illegal diversions and drying up of the creek Zannaras-Robinson could not carry on the mining, milling and development of their properties.

At this same 1949 trial Bagdad introduced Ex. N. (R. 339-343) which was an application filed by Bagdad March 24, 1939 (which was prior to the time Zannaras-Robinson or Bagdad were using any water from the creek) with the then State Water Commissioner, including a permit to commence actual construction of diversion works looking to the issuance of a Certificate of Water Right. The application proposed the diversion and use of 105,120,000 gallons of water per year. In answer to a question as to the names of the then users and the quantity available, Bagdad stated on its application: (R. 342)

“Answer to 20, above: The Old Neal Ranch, about 2 miles below the proposed point of diversion has used water from Burro Creek for irrigation purposes on a small amount of cultivated land. *This water is but a small part of that flowing, even in the dry season. The minimum flow is approximately 1,000 gpm and the Neal Ranch use will not exceed 75 gpm. For the above reason we believe that there is now in excess of 200 gpm subject to appropriation.*” Emphasis supplied.

It is to be noted that in 1939, prior to the time either Zannaras-Robinson or Bagdad were using any water

from Burro Creek, that Bagdad filed a sworn statement with the State authority that there was a minimum flow in Burro Creek of approximately 1,000 gallons per minute, even in the dry season, which is contrary to the findings of the District Court that Burro Creek is a seasonal creek wasting away in the summer months.

The State Water Commissioner then issued a permit to construct diversion works on May 5, 1939, but limited the amount, which might ripen into a certificate, to 100,000,000 gallons. (R. 343) Which clearly shows that the State Water Commissioner did not consider that there was 105,000,000 gallons available. This application and permit was not perfected by Bagdad and did not ripen into a valid appropriation.

The January 2, 1951 findings of fact, conclusion and judgment were based on evidence by Bagdad that there was at all times sufficient water in Burro Creek for both the uses of Zannaras-Robinson and Bagdad. The finding in the judgment of April 17, 1957 is directly contrary to the former. In 1957 the Court makes a finding that Burro Creek is a seasonal stream generally wasting away during the summer months.

At the 1952 trial evidence was taken, at the same hearing, on this case and on Civil Cause No. 321. That the preliminary judgment theretofore entered was not a final determination is shown by the statements by the Trial Judge in connection with the discussion of consolidation for trial when he said, "It is all the same issue," (14248 R. 52) and, "There is no original record. We are still trying 221. The Court held it in abeyance." (14248 R. 55)

At the 1952 consolidated trial Bagdad reversed its position and said that although it was pumping large



amounts of water, the lack of water at the Zannaras-Robinson point of diversion was due to natural causes. It then produced numerous witnesses. Zannaras-Robinson again showed through witnesses and photographs the lack of water.

On the basis of the evidence taken at the consolidated trial Judgment was rendered in Civil Cause No. 321, this was appealed to this Appellate Court (14248) and affirmed as reported in 229 F 2d 920. It is worthy of note that all of the evidence taken at the consolidated trial in 1952 is contained in the record of 14248 as filed with this Court. And the judgment, findings and conclusion which were affirmed by this Appellate Court, found that the shortage at the Zannaras-Robinson diversion point for five months of each year was mainly due to Bagdad's pumping and use of water above and that Zannaras-Robinson were entitled to use the amount of water adjudicated without interference from Bagdad.

It is inconceivable that the same evidence could result in contrary and conflicting judgments, especially when it is realized that the second judgment was not rendered until after the affirmance and mandate as to the former judgment.

The Bureau of Reclamation water gauge installed at the Bagdad sump measures all of the water going out of the sump down the creek *after Bagdad has pumped all of the water it wants.*

The Gauge readings were introduced at the consolidated 1952 trial for the period March through December 1949, January through December 1950, and January through August 1951, and appear as Ex. 1 of the record, printed as a separate booklet.

Mr. Dickie, Bagdad's General Manager explained the gauge readings (14248 R. 57-60). These readings show the amount of water flowing out of Bagdad's pond on Burro Creek after Bagdad pumped out water at the rate of five hundred to seven hundred gallons per minute. When the gauge reading is .0, Bagdad is pumping all the water from the creek and allowing no water to pass its pond. When the gauge reading shows the figure, for example of .25 this amounts to a discharge of 224 gallons per minute (Ex. D. 14248 R. 373). This explanation of the conversion of the gauge reading to gallons per minute was testified to by Mr. Roland F. Kaser of the Bureau of Reclamation (R. 243-245).

Printed as Appendix A of this Brief is a table containing the gauge readings converted into gallons per minute as taken from Ex. D, and also showing the total discharge of water for each month in acre feet.

Dr. Heinrich J. Thiel, a witness for Bagdad at the 1954 trial, testified that in June 1953 Bagdad pumped water from the Bagdad sump on Burro Creek at the rate of a minimum of 520 gallons per minute, (R. 454) and that from June 1952 to February 1953 at the average of 707 gallons per minute (R. 454).

Mr. Ernest R. Dickie, the General Manager for Bagdad testified at the 1954 trial that "since late in 1943, Bagdad has been pumping from the stream at its present point with a 700 capacity gallon pump" (R. 577).

Dr. Thiel also testified that during 1953 Bagdad pumped from Burro Creek at its sump 1,100 acre feet of water (R. 471) which amounts to 358,436,100 gallons of water.

Applying the pumping capacities and rate of pumping, as testified, in order to pump 358,436,100 gallons in one year the pumps must work continuously 24 hours

a day for 361 days of the year. Which clearly indicates that Burro Creek is a continuously running creek all through the year. It also shows that Bagdad diverts at least 520 gallons per minute in the summer months and at least 700 gallons per minute the rest of the year. So, when the gauge reading shows zero for June 25, 1949 until September 9, 1949 it indicates that Bagdad was pumping, for this two and a half month period, water out of the creek at the approximate rate of at least 520 gallons per minute, while no water was let down for Zannaras-Robinson.

From September 22 until September 26, 1949, the reading is zero; and from October 1 until October 19, 1949 the reading is zero. Showing that practically the same condition existed up to this time.

It should also be noted that when the reading is not zero but shows, for example, a gauge reading of .10 which corresponds to 89 gallons per minute going downstream, that Bagdad has already taken at least 700 gallons per minute beforehand—this amounts to a very small percentage of the total flow being let down for Zannaras-Robinson. These gauge readings clearly show that even during days in May 1949 Bagdad pumped out close to 80% of the flow of the creek. The year 1950 is even worse as Bagdad pumped the entire flow even during the first half of November and approximately 90% of the flow for the rest of November. As of December 5, 1950, approximately 80% of the flow was pumped out by Bagdad.

For 1951 the gauge readings show that commencing with May 28 until July 17 the reading was zero.

These gauge readings and the admitted pumping by Bagdad conclusively show that Burro Creek is a continuously running stream and completely supports the

finding of fact in Cause No. 321 that for approximately five months of each year due mainly to Bagdad's pumping operations and use above, there is no water at the Zannaras-Robinson diversion point, and conclusively shows the illegal interference by Bagdad with the natural flow of the creek, and also, as we will show, it interferes with the underflow and the natural bed of the creek.

Bagdad has excavated a pond fifteen feet deep below the natural bed of the creek in order to collect the water of Burro Creek during the summer months, and thereby pumps out the underflow in addition to the surface water. Mr. G. A. Kellis, the pump operator and caretaker at Bagdad's pumping station on Burro Creek testified to this condition (R. 279-283). This procedure was corroborated by the testimony of Bagdad's General Manager, Mr. Ernest R. Dickey, 14248 R. 284, 285).

That such interference with the natural bed of the stream and the underflow is prohibited, is discussed and is so held in the following cases:

Cole et al. vs. Richards Irrigation Co. et al. 27 Utah 205, 75 P. 376;

Loyning et al. vs. Rankin et al. (Mont. 1946) 165 P 2d 1006;

Carson et al. vs. Hayes et al. 39 Or. 97, 65 P. 814;

Willey et al. vs. Decker et al. 11 Wyo. 496, 75 P. 210.

The 1954 hearing was for the purpose of determining the form and wording of injunction against Bagdad in view of the Affirmance by this Appellate Court of the Trial Court's Decision in Civil Cause No. 321. This is shown by the Renewal of Motion to Set Cause for Hearing (R. 23-27). The motion was granted without objection by Bagdad (R. 645).

Instead, Bagdad at this point attempted to impeach and overrule the affirmed judgment in Civil Cause No. 321 by "expert testimony". While the expert testimony should have been excluded entirely we will attempt to show that the opinions of the experts were contradictory and that the opinions were not based upon personal knowledge.

A thorough discussion of the matter is found in *Irion vs. Hyde*, (Mont. 1940) 105 P 2d 666, 671, 672. It quotes with approval the case of *Gallagher vs. Kelliher*, 58 Ore. 557, 114 P 943, 944, 115 P. 596;

"A surveyor's opinion as to the result of the survey, unsupported by the details of the survey, both as to the data upon which it is based and the manner of reaching the result is not competent, but, when he gives the details of his work, it is a question of law whether his method was correct and a question of fact whether his result is correct." Citing *Seabrook v. Coos Bay Ice Co.*, 49 Ore. 237, 89 P. 417.

Dr. Heinrich J. Thiel testified as to test holes to determine the amount of the underflow which he did not make but was told about (R. 443); he testified as to the depth of the water table and the change in the creek bed *as he had been informed* (R. 418); he testified as to the permeability factor being between one thousand and ninety thousand and in the same breath said, "We don't know anything exactly" (R. 403); he testified as to the slope of the water table based upon a survey made by someone else (R. 403); and he did not even know the width of the channel actually carrying the water but had to depend on a chart prepared by someone else.

Another expert allowed to testify was Mr. Herbert C. Fletcher, in charge of research, Watershed Management, of the U. S. Forest Service, who declared that

there was no practical method for determining how much water would be lost between the Bagdad sump and the Zannaras-Robinson point of diversion (R. 532, 533). This admission was a direct contradiction of the conclusion and opinion of Dr. Thiel, as well as an attack on the method used by Dr. Thiel in arriving at a contrary conclusion.

Proof that Dr. Thiel's calculations based upon certain hypotheses are incorrect is supported by the following question and answer: (R. 492, 493)

"Q. I will ask you this question: If you had before you definite evidence on the part of the plaintiff whom we are representing, or one of its witnesses, that from April through the fall of 1950 he always saw water, running at the Kingman Crossing, and that the flow of water there varied from a thousand gallons a minute to no lower than 200 gallons a minute, would that change your view that this water couldn't run down?

"A. No; it wouldn't change my view, because it is in part ground water that is coming out at the Kingman Crossing."

It is evident from the above testimony that according to the results of the theory, assumptions, and calculations employed by Dr. Heinrich J. Thiel, that the water of Burro Creek in the summer months if not intercepted by Bagdad and allowed to run down the creek not only could not reach the Zannaras-Robinson diversion point but would not even reach the Kingman Crossing, which is three miles upstream from the Zannaras-Robinson diversion point. Since this result is diametrically opposed to the undisputed facts presented by all of the Bagdad witnesses testifying in this matter (who testified there was at all times water at the Kingman Crossing) it follows that the method assumed and data employed by the expert Dr. Thiel are

incorrect and entitled to no credence. It also confirms Dr. Fletcher's statement that exact figures are impossible of ascertainment.

It appears that Dr. Thiel professes the famous principle that if the facts do not conform to the thesis, it is the facts and not the thesis that are to blame—and woe to those who point out the facts.

Mr. Dickey, the General Manager of Bagdad, testified at the 1954 trial that Bagdad is storing in a reservoir 325,000,000 gallons of water (R. 585-587). This water is stored illegally by Bagdad without a permit from the State of Arizona, in violation of Arizona Revised Statutes Sec. 45-109.

The judgment being contrary to the weight of the evidence should be reversed and the injunction granted to Zannaras-Robinson.

This Argument is urged in support of Concise Statement of Point No. 22.

### A WATER RIGHT, BEING A PROPERTY RIGHT, CANNOT BE TAKEN WITHOUT DUE PROCESS OF LAW

Civil Cause No. 321, No. 14248 on appeal to this Appellate Court, determined the water rights of Zannaras-Robinson and decreed they were entitled to take water from Burro Creek without interference from Bagdad. The judgment in that case was based upon a finding that the lack of water at the Zannaras-Robinson point of diversion for approximately five months of each year was due mainly to the pumping operations and use of water above, by Bagdad.

Bagdad incorporated, by reference, its complaint in Civil Cause No. 321 in the answer it filed to the Zan-

naras-Robinson Amended Petition for Relief (R. 22) and also prayed for the same relief in this case as it prayed for in Civil Cause No. 321.

The District Court in the former judgment (affirmed by the Court) adjudicated the water rights according to the terms of the said rights; the application therefor and permit (14248 R. 13), the proof of appropriation (14248 R. 18) and certificate of water right (14248 R. 22), were all incorporated by reference and attached to the answer filed to Bagdad's complaint in Civil Cause No. 321.

The 1952 trial was a consolidated trial of the two cases. The issues, law and facts upon which the Court could act are so interrelated and interconnected that the two judgments must harmonize. As it stands at the present the judgment which was affirmed by this Appellate Court has been negatived and overruled.

That a water right is a property right is so basic that we will not burden the Court on that point.

All these rights, questions and terms must rest as adjudicated and determined in Civil Cause No. 321; these rights, questions and terms being pled and cross-pled by the parties in these two cases, became *res judicata*. When the case was unanimously affirmed by this Appellate Court these rights, questions and terms became the Law of the Case, by which the District Court is bound.

Kinney on Irrigation and Water Rights, Second Edition, Vol. 2, Sec. 768, page 1327 states:

“\*\*\*A perfected water right is a vested property right and its value capable of estimation in money, and one which the law protects. A water right is such a property right that it comes clearly within the Constitutional provisions that property shall not be taken



or damaged for public or private use, except upon due process of law and upon just compensation.\*\*\*”

In the present case it clearly appears that Zannaras-Robinson acquired a water right which was legally adjudicated by the District Court. The same District Court at the same consolidated trial on the same evidence then found that Bagdad was illegally taking water belonging to Zannaras-Robinson. Then the same District Court ruled in the present case that Bagdad was not taking water belonging to Zannaras-Robinson.

This amounts to the taking of property without due process of law in violation of both the State and Federal Constitutions.

#### THIS ARGUMENT IS DIRECTED TO CONCISE STATEMENT OF POINT No. 19

One of the points in issue was the water rights of the parties—Zannaras-Robinson claiming priority and Bagdad claiming priority to waters. In such instances the Court must determine relative priorities.

Kinney on Irrigation and Water Rights, 2d Ed. Vol. 3, Section 1601, page 2913, citing Platte Valley Irr. Co. v. Buckers, etc., 25 Colo. 77, 53 Pac. 334; Carlson v. City of Helena, 43 Mont. 1, 114 Pac. 110.

The Supreme Court of the State of Arizona has recognized water rights as property rights and subject to quieting under the statutes relative to quieting title to real estate. See

Salt River Valley Water Users Assn. v. Norveil, 29 Ariz. 360, 241 Pac. 503, rehearing denied 29 Ariz. 499, 242 P. 1013; Daggs v. Howard Sheep Company, 16 Ariz. 283, 145 P. 140.

Platte Valley Irr. Co. v. Buckers, *supra*, is a case wherein it was held that in an injunctive action the Court must first determine priority. To the same effect

Logan, Hyde Park & Smithfield Canal Co. v. Logan City, 72 Utah 221, 269 P. 776; Davies v. Angelo, 8 Cal. App. 305, 96 Pac. 909; Haight v. Tryon, 112 Cal. 4, 44 Pac. 318; and Cloverdale v. Smith, 128 Cal. 230, 60 Pac. 851.

While on appeal the appellate court may ordinarily presume that the trial court made a determination of the relative priorities of the parties in rendering its judgment denying an injunction, this presumption is not tenable when the statement of the trial judge is that he made no such determination. (14248 R. 54). Cash vs. Thornton, 3 Colo. App. 475, 34 P. 268.

That the matter of the relative rights of the parties is a material issue cannot be successfully refuted. If for no other reason it is material in order to make a determination as to the party upon whom the burden of proof rests. The Court erred in failing to make a determination of the relative rights of the parties and the judgment should be reversed.

## CONCLUSION

Bagdad's illegal acts in changing its method of use of water thereby recapturing, storing and reusing water formerly returned to the creek, interfering with the natural flow, underflow and the natural bed of the creek, using water for purposes other than its own mining operations by giving water to other mining companies, using more water than allowed by its Certificate of Water Right, depriving Zannaras-Robinson of water, and drying up the creek, having been established, the District Court should have recognized the Zannaras-Robinson rights on Burro Creek, Boulder Creek and its tributaries established and affirmed by this Appellate Court in Civil Cause No. 321 (thereby giving effect

to the mandate of this Appellate Court), the District Court should have enjoined the above mentioned illegal acts. The failure to properly apply the Rules of the Law of the Case and Res Judicata, failure to properly place the burden of proof upon Bagdad, and determining the judgment contrary to the weight of the evidence, results in the taking of property without due process of law, in violation of both the State and Federal Constitutions.

This case now having been before the Courts for approximately nine years, equity requires that the judgment of the District Court be reversed with directions to enter judgment for Zannaras-Robinson as prayed, in accordance with instructions of this Appellate Court.

Respectfully submitted,

MOEUR & JONES  
By Anthony O. Jones  
*Attorneys for Appellants*  
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## APPENDIX A

FEDERAL GOVERNMENT WATER GAUGES SHOWING THE WATER LEFT IN THE STREAM FLOWING AT THE RATE EXPRESSED IN GALLONS PER MINUTE AFTER BAGDAD TAKES OUT WATER CONTINUOUSLY AT THE RATE OF 520 TO 700 GALLONS PER MINUTE.

Day	1949 March		1949 April		1949 May	
	Gauge Read.	Gallons per min.	Gauge Read.	Gallons per min.	Gauge Read.	Gallons per min.
1	3.90	525131	.60	6283	.30	1077
2	2.90	228905	.65	7180	.30	1077
3	3.40	354578	.65	7180	.30	1077
4	3.60	417413	.80	9874	.30	1077
5	4.00	561040	1.30	26929	.30	1077
6	3.60	417413	1.30	26929	.30	1077
7	3.30	327648	.80	9874	.30	1077
8	3.20	300718	.80	9874	.30	1077
9	2.50	157091	.70	8078	.30	1077
10	2.70	192997	.70	8078	.30	1077
11	3.20	300718	.60	6283	.30	1077
12	3.00	246858	.60	6283	.30	1077
13	1.90	78995	.60	6283	.30	1077
14	1.50	35907	.60	6283	.20	179
15	1.40	31417	.60	6283	.20	179
16	1.50	35907	.50	4488	.30	1077
17	1.40	31417	.50	4488	.30	1077
18	1.30	26929	.50	4488	.30	1077
19	1.30	26929	.50	4488	.30	1077
20	1.30	26929	.50	4488	.40	2782
21	1.20	22441	.50	4488	.40	2782
22	1.20	22441	.40	2782	.30	1077
23	1.10	17953	.40	2782	.30	1077
24	.90	11669	.30	2077	.30	1077
25	.60	6283	.30	1077	.20	179
26	.70	8078	.30	1077	.20	179
27	.60	6283	.30	1077	.20	179
28	.60	6283	.30	1077	.20	179
29	.60	6283	.30	1077	.20	179
30	.60	6283	.30	1077	.20	179
31	.60	6283			.20	179
		4445200		191725		28715

acre-feet  
er month

4445200x60x24 = 19635.2  
325851

191725x60x24 = 846.8  
325851

28715x60x24 = 126.8  
325851

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Day	1949 June		1949 July		1949 August	
	Gauge Read.	Gallons per min.	Gauge Read.	Gallons per min.	Gauge Read.	Gallons per min.
1	.10	89	.0	0	.0	0
2	.10	89	.0	0	.0	0
3	.10	89	.0	0	.0	0
4	.10	89	.0	0	.0	0
5	.10	89	.0	0	.0	0
6	.20	179	.0	0	.0	0
7	.30	1077	.0	0	.0	0
8	.30	1077	.0	0	.0	0
9	.30	1077	.0	0	.0	0
10	.30	1077	.0	0	.0	0
11	.30	1077	.0	0	.0	0
12	.30	1077	.0	0	.0	0
13	.30	1077	.0	0	.0	0
14	.30	1077	.0	0	.0	0
15	.30	1077	.0	0	.0	0
16	.30	1077	.0	0	.0	0
17	.30	1077	.0	0	.0	0
18	.20	179	.0	0	.0	0
19	.20	179	.0	0	.0	0
20	.20	179	.0	0	.0	0
21	.20	179	.0	0	.0	0
22	.20	179	.0	0	.0	0
23	.20	179	.0	0	.0	0
24	.20	179	.0	0	.0	0
25	.0	0	.0	0	.0	0
26	.0	0	.0	0	.0	0
27	.0	0	.0	0	.0	0
28	.0	0	.0	0	.0	0
29	.0	0	.0	0	.0	0
30	.0	0	.0	0	.0	0
31			.0	0	.0	0
		13724		0		0
Acre-feet		13724x60x24		0		0
per month		325851 = 60.6				

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Day	1949 September		1949 October		1949 November	
	Gauge Read.	Gallons per min.	Gauge Read.	Gallons per min.	Gauge Read.	Gallons per min.
1	.0	0	.0	0	.30	1077
2	.0	0	.0	0	.30	1077
3	.0	0	.0	0	.30	1077
4	.0	0	.0	0	.30	1077
5	.0	0	.0	0	.30	1077
6	.0	0	.0	0	.30	1077
7	.0	0	.0	0	.30	1077
8	.0	0	.0	0	.30	1077
9	.0	0	.0	0	.30	1077
10	.30	1077	.0	0	.40	2782
11	.30	1077	.0	0	.40	2782
12	.30	1077	.0	0	.40	2782
13	.20	179	.0	0	.40	2782
14	.20	179	.0	0	.40	2782
15	.20	179	.0	0	.40	2782
16	.20	179	.0	0	.40	2782
17	.20	179	.0	0	.40	2782
18	.20	179	.0	0	.40	2782
19	.20	179	.0	0	.40	2782
20	.10	89	.30	1077	.40	2782
21	.10	89	.30	1077	.40	2782
22	.0	0	.30	1077	.30	1077
23	.0	0	.30	1077	.40	2782
24	.0	0	.30	1077	.40	2782
25	.0	0	.30	1077	.30	1077
26	.0	0	.30	1077	.30	1077
27	.20	179	.30	1077	.30	1077
28	.20	179	.30	1077	.30	1077
29	.20	179	.30	1077	.30	1077
30	.10	89	.30	1077	.40	2782
31	.10	89	.30	1077		
		5377		12924		57885
Acre-feet per month	5377x60x24 325851 = 23.7		12924x60x24 325851 = 57.0		57885x60x24 325851 = 255.7	

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FEDERAL GOVERNMENT WATER GAUGES SHOWING THE WATER LEFT IN THE STREAM FLOWING AT THE RATE EXPRESSED IN GALLONS PER MINUTE AFTER BAGDAD TAKES OUT WATER CONTINUOUSLY AT THE RATE OF 520 TO 700 GALLONS PER MINUTE.

Day	1949 February		1950 January		1950 December	
	Gauge Read.	Gallons per min.	Gauge Read.	Gallons per min.	Gauge Read.	Gallons per min.
1	.30	1077	.40	2782	.50	4488
2	.30	1077	.40	2782	.50	4488
3	.30	1077	.50	4488	.50	4488
4	.40	2782	.50	4488	.50	4488
5	.40	2782	.40	2782	.50	4488
6	.40	2782	.40	2782	.50	4488
7	.40	2782	.40	2782	.40	2782
8	.40	2782	.40	2782	.40	2782
9	.40	2782	.40	2782	.50	4488
10	.50	4488	.40	2782	.50	4488
11	.50	4488	.40	2782	.50	4488
12	.50	4488	.40	2782	.50	4488
13	.50	4488	.40	2782	.40	2782
14	.50	4488	.40	2782	.40	2782
15	.50	4488	.40	2782	.40	2782
16	.50	4488	.40	2782	.40	2782
17	.50	4488	.40	2782	.40	2782
18	.50	4488	.40	2782	.40	2782
19	.50	4488	.40	2782	.40	2782
20	.50	4488	.40	2782	.40	2782
21	.50	4488	.40	2782	.40	2782
22	.50	4488	.40	2782	.40	2782
23	.40	2782	.40	2782	.40	2782
24	.40	2782	.40	2782	.30	1077
25	.40	2782	.40	2782	.30	1077
26	.40	2782	.40	2782	.40	2782
27	.40	2782	.40	2782	.40	2782
28	.40	2782	.50	4488	.50	4488
29	.40	2782	.50	4488		
30	.40	2782	.50	4488		
31	.40	2782	.50	4488		
		103305		96478		93252
Acre-feet per month	103305x60x24 325851 = 456.3		96478x60x24 325851 = 423.1		93252x60x24 325851 = 411.9	

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Day	1950 March		1950 April		1950 May	
	Gauge Read.	Gallons per min.	Gauge Read.	Gallons per min.	Gauge Read.	Gallons per min.
1	.50	4488	.40	2782	.20	179
2	.50	4488	.40	2782	.20	179
3	.50	4488	.40	2782	.20	179
4	.50	4488	.40	2782	.20	179
5	.50	4488	.40	2782	.20	179
6	.40	2782	.40	2782	.20	179
7	.40	2782	.40	2782	.20	179
8	.40	2782	.40	2782	.20	179
9	.40	2782	.40	2782	.20	179
10	.40	2782	.40	2782	.20	179
11	.40	2782	.40	2782	.20	179
12	.40	2782	.40	2782	.20	179
13	.40	2782			.20	179
14	.40	2782			.20	179
15	.40	2782	.40	2782	.15	134
16	.40	2782	.30	1077	.15	134
17	.30	1077	.30	1077	.15	134
18	.30	1077	.30	1077	.15	134
19	.30	1077	.30	1077	.15	134
20	.30	1077	.30	1077	.15	134
21	.30	1077	.30	1077	.15	134
22	.30	1077	.30	1077	.15	134
23	.30	1077	.20	179	.10	89
24	.30	1077	.20	179	.10	89
25	.45	3635	.20	179	.10	89
26	.45	3635	.20	179	.10	89
27	.45	3635	.20	179	.10	89
28	.45	3635	.20	179	.10	89
29	.45	3635	.20	179	.10	89
30	.45	3635	.20	179	.10	89
31	.40	2782			.10	89
		86250		45137		4379

Acre-feet per month       $86250 \times 60 \times 24 \div 325851 = 380.9$        $45137 \times 60 \times 24 \div 325851 = 199.3$        $4379 \times 60 \times 24 \div 325851 = 19.3$



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Day	1950 June		1950 July		1950 August	
	Gauge Read.	Gallons per min.	Gauge Read.	Gallons per min.	Gauge Read.	Gallons per min.
1	.0	0	.0	0	.20	179
2	.0	0	.0	0	.20	179
3	.0	0	.0	0	.20	179
4	.0	0	.0	0	.20	179
5	.0	0	.0	0	.30	1077
6	.0	0	.0	0	.20	179
7	.0	0	.0	0	.20	179
8	.0	0	.10	89	.20	179
9	.0	0	.10	89	.20	179
10	.0	0	.10	89	.20	179
11	.0	0	.10	89	.20	179
12	.0	0	.0	0	.20	179
13	.0	0	.0	0	.10	89
14	.0	0	.0	0	.10	89
15	.0	0	.0	0	.10	89
16	.0	0	.0	0	.10	89
17	.0	0	.0	0	.10	89
18	.0	0	.0	0	.0	0
19	.0	0	.0	0	.0	0
20	.0	0	.0	0	.0	0
21	.0	0	.0	0	.0	0
22	.0	0	.0	0	.0	0
23	.0	0	.0	0	.0	0
24	.0	0	.50	4488	.10	89
25	.0	0	.50	4488	.10	89
26	.0	0	.40	2782	.10	89
27	.0	0	.30	1077	.10	89
28	.0	0	.30	1077	.0	0
29	.0	0	.20	179	.0	0
30	.0	0	.20	179	.0	0
31	.0	0	.20	179	.0	0
				14805	3847	

Acre-feet  
per month  $14805 \times 60 \times 24 = 65.3$   
325851

$3847 \times 60 \times 24 = 16.9$   
325851

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Day	1950 September		1950 October		1950 November	
	Gauge Read.	Gallons per min.	Gauge Read.	Gallons per min.	Gauge Read.	Gallons per min.
1	.0	0	.10	89	.0	0
2	.0	0	.10	89	.0	0
3	.0	0	.10	89	.0	0
4	.0	0	.10	89	.0	0
5	.10	89	.10	89	.0	0
6	.20	179	.10	89	.0	0
7	.50	4488	.10	89	.0	0
8	.65	7180	.10	89	.0	0
9	.50	4488	.10	89	.0	0
10	.30	1077	.10	89	.0	0
11	.30	1077	.10	89	.0	0
12	.30	1077	.10	89	.0	0
13	.10	89	.10	89	.0	0
14	.10	89	.10	89	.0	0
15	.10	89	.0	0	.0	0
16	.10	89	.0	0	.0	0
17	.10	89	.0	0	.0	0
18	.10	89	.0	0	.0	0
19	.10	89	.0	0	.10	89
20	.10	89	.0	0	.10	89
21	.10	89	.0	0	.10	89
22	.10	89	.0	0	.10	89
23	.10	89	.0	0	.10	89
24	.10	89	.0	0	.10	89
25	.10	89	.0	0	.10	89
26	.10	89	.0	0	.10	89
27	.10	89	.0	0	.10	89
28	.10	89	.0	0	.10	89
29	.10	89	.0	0	.10	89
30	.10	89	.0	0	.10	89
31			.0	0		
		21537		1246		1068

Acre-feet per month     $21537 \times 60 \times 24 \div 325851 = 95.1$      $1246 \times 60 \times 24 \div 325851 = 5.5$      $1068 \times 60 \times 24 \div 325851 = 4.7$

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Day	1950 December		1951 January		1951 February	
	Gauge Read.	Gallons per min.	Gauge Read.	Gallons per min.	Gauge Read.	Gallons per min.
1	.15	134	.40	2782	.60	6283
2	.15	134	.40	2782	.55	5285
3	.15	134	.40	2782	.50	4488
4	.20	179	.40	2782	.45	3635
5	.20	179	.40	2782	.45	3635
6	.25	224	.40	2782	.45	3635
7	.30	1077	.40	2782	.45	3635
8	.30	1077	.40	2782	.40	2782
9	.35	1924	.40	2782	.40	2782
10	.35	1924	.40	2782	.40	2782
11	.35	1924	.45	3635	.40	2782
12	.35	1924	.45	3635	.40	2782
13	.35	1924	.45	3635	.40	2782
14	.35	1924	.45	3635	.40	2782
15	.35	1924	.45	3635	.40	2782
16	.35	1924	.45	3635	.40	2782
17	.35	1924	.45	3635	.40	2782
18	.35	1924	.40	2782	.40	2782
19	.35	1924	.40	2782	.40	2782
20	.35	1924	.40	2782	.40	2782
21	.40	2782	.40	2782	.40	2782
22	.40	2782	.40	2782	.40	2782
23	.40	2782	.40	2782	.40	2782
24	.40	2782	.40	2782	.40	2782
25	.40	2782	.45	3635	.40	2782
26	.40	2782	.45	3635	.40	2782
27	.40	2782	.45	3635	.40	2782
28	.40	2782	.50	4488	.40	2782
29	.40	2782	.50	4488		
30	.40	2782	.50	4488		
31	.40	2782	.50	4488		
		56828		101596		89018

56828x60x24 = 251.0    101596x60x24 = 448.7    89018x60x24 = 393.  
 325851                      325851                      325851

## APPENDIX A

FEDERAL GOVERNMENT WATER GAUGES SHOWING THE WATER LEFT IN THE STREAM FLOWING AT THE RATE EXPRESSED IN GALLONS PER MINUTE AFTER BAGDAD TAKES OUT WATER CONTINUOUSLY AT THE RATE OF 520 TO 700 GALLONS PER MINUTE.

Day	1951 March		1951 April		1951 May	
	Gauge Read.	Gallons per min.	Gauge Read.	Gallons per min.	Gauge Read.	Gallons per min.
1	.40	2782	.35	1924	.45	3635
2	.40	2782	.35	1924	.40	2782
3	.40	2782	.40	2782	.40	2782
4	.40	2782	.50	4488	.40	2782
5	.40	2782	.50	4488	.35	1924
6	.40	2782	.45	3635	.35	1924
7	.40	2782	.40	2782	.30	1077
8	.40	2782	.40	2782	.30	1077
9	.40	2782	.40	2782	.30	1077
10	.40	2782	.40	2782	.25	224
11	.40	2782	.40	2782	.25	224
12	.40	2782	.40	2782	.25	224
13	.40	2782	.35	1924	.25	224
14	.40	2782	.35	1924	.30	1077
15	.40	2782	.30	1077	.35	1924
16	.40	2782	.30	1077	.40	2782
17	.40	2782	.30	1077	.40	2782
18	.40	2782	.30	1077	.35	1924
19	.40	2782	.30	1077	.35	1924
20	.40	2782	.35	1924	.30	1077
21	.40	2782	.35	1924	.30	1077
22	.40	2782	.30	1077	.30	1077
23	.35	1924	.30	1077	.30	1077
24	.35	1924	.30	1077	.25	224
25	.35	1924	.25	224	.20	179
26	.35	1924	.35	1924	.10	89
27	.35	1924	.40	2782	.10	89
28	.35	1924	.40	2782	.0	0
29	.35	1924	.40	2782	.0	0
30	.35	1924	.40	2782	.0	0
31	.35	1924			.0	0
		78520		68303		37258

cre-feet  
 r month

78520x60x24  
 325851 = 346.8

68303x60x24  
 325851 = 301.7

37258x60x24  
 325851 = 164.5

## APPENDIX A

FEDERAL GOVERNMENT WATER GAUGES SHOWING THE WATER LEFT IN THE STREAM FLOWING AT THE RATE EXPRESSED IN GALLONS PER MINUTE AFTER BAGDAD TAKES OUT WATER CONTINUOUSLY AT THE RATE OF 520 TO 700 GALLONS PER MINUTE.

Day	1951 June		1951 July	
	Gauge Read.	Gallons per min.	Gauge Read.	Gallons per min.
1	.0	0	.0	0
2	.0	0	.0	0
3	.0	0	.0	0
4	.0	0	.0	0
5	.0	0	.0	0
6	.0	0	.0	0
7	.0	0	.0	0
8	.0	0	.0	0
9	.0	0	.0	0
10	.0	0	.0	0
11	.0	0	.0	0
12	.0	0	.0	0
13	.0	0	.0	0
14	.0	0	.0	0
15	.0	0	.0	0
16	.0	0	.0	0
17	.0	0	.0	0
18	.0	0	.20	179
19	.0	0	.30	1077
20	.0	0	.0	0
21	.0	0	.0	0
22	.0	0	.50	4488
23	.0	0	.30	1077
24	.0	0	.10	89
25	.0	0	.10	89
26	.0	0	.10	89
27	.0	0	.10	89
28	.0	0	.20	179
29	.0	0	.70	8078
30	.0	0	.30	1077
31			.20	179
		0		16930

Acre-feet  
per month

$$\frac{16930 \times 60 \times 24}{325851} = 74.7$$

APPENDIX

THE FOLLOWING TABLES SHOW THE RESULTS OF THE ANALYSES OF THE SAMPLES OF THE SEVERAL TYPES OF COAL WHICH WERE ANALYZED AT THE U. S. GEOLOGICAL SURVEY LABORATORY, WASHINGTON, D. C. IN 1901.

Sample	Proximate Analysis	Ultimate Analysis	Heating Value
1	85.0	85.0	14,500
2	85.0	85.0	14,500
3	85.0	85.0	14,500
4	85.0	85.0	14,500
5	85.0	85.0	14,500
6	85.0	85.0	14,500
7	85.0	85.0	14,500
8	85.0	85.0	14,500
9	85.0	85.0	14,500
10	85.0	85.0	14,500
11	85.0	85.0	14,500
12	85.0	85.0	14,500
13	85.0	85.0	14,500
14	85.0	85.0	14,500
15	85.0	85.0	14,500
16	85.0	85.0	14,500
17	85.0	85.0	14,500
18	85.0	85.0	14,500
19	85.0	85.0	14,500
20	85.0	85.0	14,500
21	85.0	85.0	14,500
22	85.0	85.0	14,500
23	85.0	85.0	14,500
24	85.0	85.0	14,500
25	85.0	85.0	14,500
26	85.0	85.0	14,500
27	85.0	85.0	14,500
28	85.0	85.0	14,500
29	85.0	85.0	14,500
30	85.0	85.0	14,500
31	85.0	85.0	14,500
32	85.0	85.0	14,500
33	85.0	85.0	14,500
34	85.0	85.0	14,500
35	85.0	85.0	14,500
36	85.0	85.0	14,500
37	85.0	85.0	14,500
38	85.0	85.0	14,500
39	85.0	85.0	14,500
40	85.0	85.0	14,500
41	85.0	85.0	14,500
42	85.0	85.0	14,500
43	85.0	85.0	14,500
44	85.0	85.0	14,500
45	85.0	85.0	14,500
46	85.0	85.0	14,500
47	85.0	85.0	14,500
48	85.0	85.0	14,500
49	85.0	85.0	14,500
50	85.0	85.0	14,500

No. 15640

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**United States**  
**Court of Appeals**  
for the Ninth Circuit

---

JOHN PHILLIP ZANNARAS, J. P. ROBIN-  
SON, JR., and U. S. TUNGSTEN CORPO-  
RATION,

Appellants,

vs.

BAGDAD COPPER CORPORATION, a Corpora-  
tion,

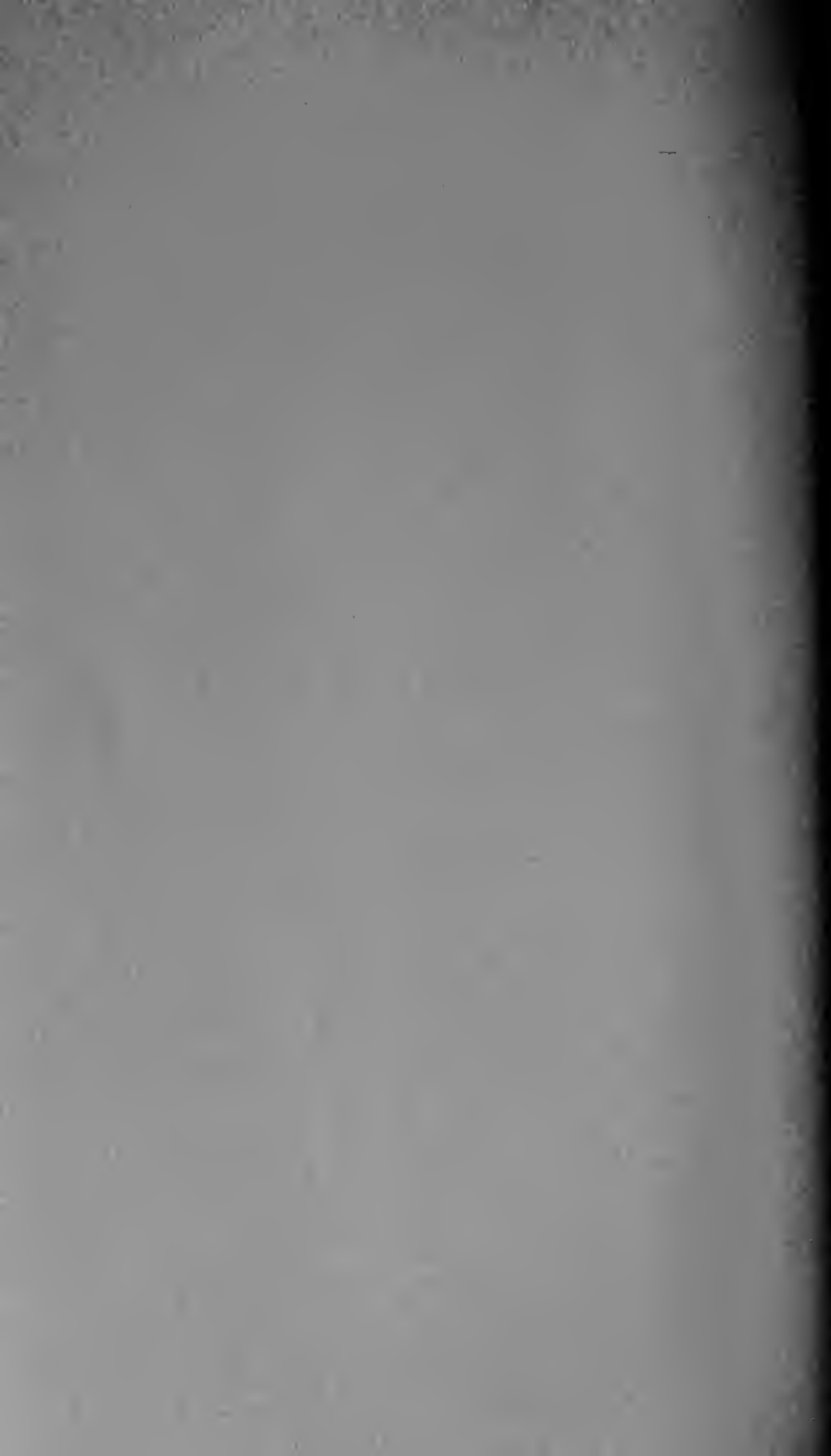
Appellee.

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**Supplemental**  
**Transcript of Record**

---

**Appeal from the United States District Court for the**  
**District of Arizona**





No. 15640

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**United States  
Court of Appeals**  
for the Ninth Circuit

---

JOHN PHILLIP ZANNARAS, J. P. ROBIN-  
SON, JR., and U. S. TUNGSTEN CORPO-  
RATION,

Appellants,

vs.

BAGDAD COPPER CORPORATION, a Corpora-  
tion,

Appellee.

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**Supplemental  
Transcript of Record**

---

**Appeal from the United States District Court for the  
District of Arizona**



# PLAINTIFF'S EXHIBIT No. 1

(Admitted and Filed May 13, 1952.)

## Burro Creek Water Gauge Readings

March, 1949

Date	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	
Gauge Reading....	3.90	2.90	3.40	3.60	4.00	3.60	3.30	3.20	2.50	2.70	3.20	3.00	1.90	1.50	1.40	
Date	16	17	18	19	20	21	22	23	24	25	26	27	28	29	30	31
Gauge Reading....	1.50	1.40	1.30	1.30	1.30	1.20	1.20	1.10	0.90	.80	.70	.60	.60	.60	.60	.60

## Burro Creek Water Gauge Reading

for April, 1949

Date	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
Gauge Reading.....	0.60	0.65	0.65	0.80	1.30	1.30	0.80	0.80	0.70	0.70	0.60	0.60	0.60	0.60	0.60
Date	16	17	18	19	20	21	22	23	24	25	26	27	28	29	30
Gauge Reading.....	0.50	0.50	0.50	0.50	0.50	0.50	0.40	0.40	0.30	0.30	0.30	0.30	0.30	0.30	0.30

## Plaintiff's Exhibit No. 1—(Continued)

## Burro Creek Water Gauge Readings

for September, 1949

Date	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
Gauge Reading	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.30	0.30	0.30	0.20	0.20	0.20
Date	16	17	18	19	20	21	22	23	24	25	26	27	28	29	30
Gauge Reading	0.20	0.20	0.20	0.10	0.10	0.10	0.00	0.00	0.00	0.00	0.20	0.20	0.20	0.10	0.10

# Water Report for October, 1949

[illegible]

Bagdad Copper Corporation  
Bagdad, Arizona

Water Report  
for November, 1949

Date	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
Gauge Reading.....	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.40	0.40	0.40	0.40	0.40	0.40
Date	16	17	18	19	20	21	22	23	24	25	26	27	28	29	30
Gauge Reading....	0.40	0.40	0.40	0.40	0.40	0.40	0.30	0.40	0.40	0.30	0.30	0.30	0.30	0.30	0.40

Bagdad Copper Corporation  
Bagdad, Arizona

January 1, 1950.

December Water Report

Date	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
Gauge Reading.....	0.30	0.30	0.30	0.40	0.40	0.40	0.40	0.40	0.40	0.50	0.50	0.50	0.50	0.50	0.50
Date	16	17	18	19	20	21	22	23	24	25	26	27	28	29	30
Gauge Reading....	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40

	31
Gauge Reading....	0.40



Bagdad Copper Corporation  
Bagdad, Arizona

August 5, 1950.

July Water Reading

Date	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
Gauge Reading....	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.10	0.10	0.10	0.10	0.0	0.0	0.0	0.0
Date	16	17	18	19	20	21	22	23	24	25	26	27	28	29	30
Gauge Reading....	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.50	0.50	0.40	0.30	0.30	0.20	0.20
															31

Burro Creek—Bill Williams River

August Water Reading

Date	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
Gauge Reading....	0.20	0.20	0.20	0.20	0.30	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.10	0.10	0.10
Date	16	17	18	19	20	21	22	23	24	25	26	27	28	29	30
Gauge Reading....	0.10	0.10	0.0	0.0	0.0	0.0	0.0	0.0	0.10	0.10	0.10	0.10	0.0	0.0	0.0
															31





Bagdad Copper Corporation  
Bagdad, Arizona

Water Reading—Month of March, 1951

Date	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	
Gauge Reading....	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	
Date	16	17	18	19	20	21	22	23	24	25	26	27	28	29	30	31
Gauge Reading....	0.40	0.40	0.40	0.40	0.40	0.40	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.35

Bagdad Copper Corporation  
Bagdad, Arizona

Water Reading—Month of April, 1951

Date	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
Gauge Reading....	0.35	0.35	0.40	0.50	0.50	0.45	0.45	0.40	0.40	0.40	0.40	0.40	0.35	0.35	0.30
Date	16	17	18	19	20	21	22	23	24	25	26	27	28	29	30
Gauge Reading....	0.30	0.30	0.30	0.30	0.35	0.35	0.30	0.30	0.30	0.25	0.35	0.40	0.40	0.40	0.40

## Plaintiff's Exhibit No. 1—(Continued)

Bagdad Copper Corporation  
Bagdad, Arizona

## Water Reading August, 1951

Date	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	
Gauge Reading.....	0.10	0.10	2.00	4.20	1.30	1.20	0.56	0.40	0.40	0.30	0.25	0.20	0.20	0.20	0.10	
			6 A.M.	4												
			9 P.M.	12 A.M.												
			4.2	3.0	6 1/2'											
Date	16	17	18	19	20	21	22	23	24	25	26	27	28	29	30	31
Gauge Reading.....	1.10		0.70	0.30	0.35	0.30	0.40	0.30	0.70	0.30	0.40	0.30	0.35	15-ft.	4-ft.	x
								6 A.M.								
								11 A.M.								
								1.20								

No. 15642

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**United States  
Court of Appeals**  
for the Ninth Circuit

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**ALBERT DEL GUERCIO**, Officer in Charge, Im-  
migration and Naturalization Service, Los An-  
geles, Calif.,

Appellant,

vs.

**BENNIE SEVITT**,

Appellee.

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**Transcript of Record**

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**Appeal from the United States District Court for the  
Southern District of California,  
Central Division.**

**FILED**

SEP 13 1957

**PAUL E. GORDEN, CLERK**



No. 15642

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**United States  
Court of Appeals**  
for the Ninth Circuit

---

**ALBERT DEL GUERCIO**, Officer in Charge, Immigration and Naturalization Service, Los Angeles, Calif.,

Appellant,

vs.

**BENNIE SEVITT**,

Appellee.

---

**Transcript of Record**

---

**Appeal from the United States District Court for the  
Southern District of California,  
Central Division.**

SHREVEPORT

1915  
JAN 10 1915

1915  
JAN 10 1915

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

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## NAMES AND ADDRESSES OF ATTORNEYS

### For Appellant:

LAUGHLIN E. WATERS,  
United States Attorney;

RICHARD A. LAVINE,  
Assistant U. S. Attorney, Chief of Civil  
Division;

BRUCE A. BEVAN, JR.,  
Assistant U. S. Attorney,  
600 Federal Building,  
Los Angeles 12, California.

### For Appellee:

WIRIN, RISSMAN & OKRAND,  
257 South Spring Street,  
Los Angeles 12, California.



In the United States District Court, Southern  
District of California, Central Division

No. 19588

BENNIE SEVITT,

Plaintiff,

vs.

ALBERT DEL GUERCIO, Officer in Charge, Im-  
migration and Naturalization Service, Los An-  
geles, California,

Defendant.

### COMPLAINT

(For Injunction and Declaratory Judgment)

Plaintiff alleges:

#### I.

Plaintiff, Bennie Sevitt, is a resident of Los Angeles, California. He is a native and citizen of Ireland.

#### II.

Defendant, Albert Del Guercio, is the duly appointed and acting Officer in Charge of the Immigration and Naturalization Service, United States Department of Justice, for the Los Angeles area. Defendant is charged with the administration and enforcement of the immigration and naturalization laws of the United States within said area and within the Southern District of California.

#### III.

This action is filed to restrain and enjoin defendant and [2\*] his agents from enforcing or other-

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\*Page numbering appearing at foot of page of original Certified Transcript of Record.

wise carrying into effect an Order and Warrant of Deportation heretofore made, entered and issued against plaintiff, upon the ground that said Order and Warrant was, at all times herein, and still is, void, illegal and contrary to the law and evidence.

#### IV.

This Court has jurisdiction by virtue of the Administrative Procedures Act (5 USC 1001-1011), particularly Section 10 thereof (5 USC 1009), by virtue of Section 242(e) of the Immigration and Nationality Act, 1952 (8 USC 1252(e)), and by virtue of the Declaratory Judgments Act (28 USC 2201, et seq.), to declare said Order and Warrant unlawful, illegal and void, to vacate said Order and Warrant and terminate the within deportation proceedings and to restrain and enjoin defendant and his agents from executing or otherwise acting upon an unlawful and illegal Order and Warrant of Deportation.

#### V.

On or about March 24, 1954, plaintiff was served with a Warrant of Arrest and charged with being subject to deportation as an alien who, after his legal admission into the United States as a visitor for pleasure, failed to comply with the conditions of such status.

#### VI.

Subsequent to said arrest, hearings were held. During the course of said hearings an additional charge was lodged to the effect that plaintiff was subject to deportation as an alien who failed to fur-

nish address information as required by Section 265 of the Immigration and Nationality Act. Said additional charge was lodged despite the fact that, plaintiff is informed and believes and therefore alleges, the Immigration and Naturalization Service had knowledge of the alleged failure to furnish address information before and at the time it served the aforesaid Warrant of Arrest upon plaintiff. [3]

On or about December 8, 1955, a Special Inquiry Officer of the Immigration and Naturalization Service determined that plaintiff was subject to deportation and entered an order that plaintiff be deported.

Appeal from said decision and order was taken to the Board of Immigration Appeals, which Board, on or about January 24, 1956, dismissed the appeal, as a consequence of which said Order of Deportation became final and remains in full force and effect.

## VII.

During said proceedings plaintiff filed timely applications for suspension of deportation and/or voluntary departure. Said applications were denied by the Board of Immigration Appeals not because of the exercise of discretion by said Board but because the Board refused, failed and did not exercise its discretion. The Board of Immigration Appeals, plaintiff is informed and believes, and therefore alleges, is the body duly authorized, empowered and delegated by the Attorney General of the United States to exercise the power to suspend deportation

and to authorize voluntary departure under the Immigration and Nationality Act, 1952.

Accordingly plaintiff has exhausted his administrative remedies. Plaintiff has been permitted to remain out of custody, on bond.

### VIII.

On or about February 9, 1956, plaintiff received by Certified Mail from the office of defendant a written notice that arrangements to effect the deportation of plaintiff pursuant to the aforesaid order of deportation were being made.

### IX.

Said Order of Deportation, the Findings of Fact and Conclusions of Law upon which said Order is based, and the administrative proceedings and action by the Immigration and Naturalization Service which have been sought and seek to effect plaintiff's deportation [4] are unlawful, illegal and void for the following reasons:

(1) The Finding, Conclusion and Order that plaintiff is deportable as an alien who failed to furnish address information as required by Section 265 of the Immigration and Nationality Act are not based upon, and are contrary to, reliable, reasonable, substantial and probative evidence, and is therefore contrary to plaintiff's right to Due Process of Law and to the Administrative Procedures Act and the Immigration and Nationality Act of 1952.

(2) The refusal and failure of the Board of Immigration Appeals to exercise its discretion as to whether plaintiff should be allowed suspension of deportation and/or voluntary departure is contrary to the Immigration and Nationality Act and to plaintiff's right to Due Process of Law.

X.

Plaintiff has no plain, speedy or otherwise adequate remedy at law, and unless defendant is restrained and enjoined by this Court, plaintiff will be placed beyond the jurisdiction of this or any Court of the United States and thereby suffer irreparable harm.

Wherefore, plaintiff prays judgment as follows:

1. For an injunction restraining and enjoining the defendant, his agents, servants, employees, representatives, and all persons acting under his direction or control, or in concert with him, from deporting plaintiff, or causing or attempting to cause the deportation of plaintiff under or by virtue of the Order or Warrant of Deportation herein;

2. Pending the hearing and determination of this action, for a temporary injunction and restraining order restraining and enjoining the defendant, his agents, servants, employees, representatives, and all persons acting or serving under his direction or control, or in concert with him, from deporting plaintiff, or causing or attempting to cause the deportation of plaintiff under or by virtue [5] of the

Order or Warrant of Deportation herein; and for such other and further relief as may be appropriate to preserve the status and rights of the parties herein pending the conclusion of these proceedings;

3. Declaring said Order and Warrant of Deportation void, illegal and contrary to law, and of no force or effect, and vacating or setting aside said Order and Warrant;

4. Declaring the deportation proceedings against plaintiff to be void, illegal and contrary to law, and of no force or effect, and terminating, vacating, setting aside and dismissing said deportation proceedings;

5. Or, in the alternative to Paragraphs 3 and 4 of this prayer, declaring said Order and Warrant of Deportation void, illegal and contrary to law, and of no force or effect, unless and until the Attorney General of the United States or the Board of Immigration Appeals exercise their, his or its discretion as to whether to grant plaintiff suspension of deportation and/or voluntary departure;

6. For such other and further relief as to the Court may seem just and proper.

WIRIN, RISSMAN & OKRAND,

By /s/ FRED OKRAND,

Attorneys for Plaintiff.

Duly verified.

[Endorsed]: Filed March 2, 1956. [6]



[Title of District Court and Cause.]

ANSWER

Comes Now the defendant, Albert Del Guercio, Officer in Charge, Immigration and Naturalization Service, Los Angeles, California, by his attorneys, Laughlin E. Waters, United States Attorney for the Southern District of California; Max F. Deutz and Volney V. Brown, Jr., Assistants United States Attorney for the same District, and for answer to the Complaint on file herein admits, denies and alleges as follows:

I.

Admits the allegations contained in Paragraphs I, II, V, VII and VIII.

II.

Denies each and every allegation contained in Paragraphs III and IX. [8]

III.

Admits the allegations contained in Paragraph VI, except denies that said additional charge was lodged despite the fact that the Immigration and Naturalization Service had knowledge of the alleged failure to furnish address information before or at the time it served the Warrant of Arrest upon plaintiff.

Wherefore, defendant prays that the relief prayed for in the said Complaint be denied, that the decision of the Special Inquiry Officer be affirmed, that

this Court order that plaintiff be deported from the United States in the manner provided by law on the charge contained in the Warrant of Arrest heretofore issued by the Immigration and Naturalization Service, that defendant recover his costs and disbursements herein incurred, and for such other and further relief as may be equitable and proper.

LAUGHLIN E. WATERS,  
United States Attorney;

MAX F. DEUTZ,  
Assistant U. S. Attorney,  
Chief of Civil Division;

VOLNEY V. BROWN, JR.,  
Assistant U. S. Attorney,  
Attorneys for Defendant.

Affidavit of Service by Mail attached.

[Endorsed]: Filed April 19, 1956. [9]

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[Title of District Court and Cause.]

### PRETRIAL ORDER

At a conference held under Rule 16, F.R.C.P., by direction of William M. Byrne, Judge, the following admissions and agreements of fact were made by the parties and require no proof:

(1) Plaintiff, Bennie Sevitt, is a resident of Los Angeles, California. He is a native and citizen of Ireland. He is thirty-seven years old.

(2) Defendant, Albert Del Guercio, is the duly appointed and acting Officer in Charge of the Immigration and Naturalization Service, United States Department of Justice, for the Los Angeles area. Defendant is charged with the administration and enforcement of the immigration and naturalization laws of the United States within said area and within the Southern District of California.

(3) This Court has jurisdiction by virtue of the Administrative [11] Procedures Act (5 USC 1001-1011), particularly Section 10 thereof (5 USC 1009), by virtue of Section 242 (3) of the Immigration and Nationality Act, 1952 (8 USC 1252 (e)), and by virtue of the Declaratory Judgments Act (28 USC 2201, et seq.), to declare said Order and Warrant unlawful, illegal and void, to vacate said Order and Warrant and terminate the within deportation proceeding and to restrain and enjoin defendant and his agents from executing or otherwise acting upon an unlawful and illegal Order and Warrant of Deportation.

(4) On or about March 24, 1954, plaintiff was served with a Warrant of Arrest and charged with being subject to deportation as an alien who, after his legal admission into the United States as a visitor for pleasure, failed to comply with the conditions of such status.

(5) Subsequent to said arrest, hearings were held. During the course of said hearings an additional charge was lodged to the effect that plaintiff

was subject to deportation as an alien who failed to furnish address information as required by Section 265 of the Immigration and Nationality Act.

On or about December 8, 1955, a Special Inquiry Officer of the Immigration and Naturalization Service determined that plaintiff was subject to deportation on both grounds and entered an order that plaintiff be deported.

Appeal from said decision and order was taken to the Board of Immigration Appeals, which Board, on or about January 24, 1956, dismissed the appeal, as a consequence of which said Order of Deportation became final and remains in full force and effect.

(6) During said proceedings plaintiff filed timely applications for suspension of deportation and/or voluntary departure. Said applications were denied by the Board of Immigration Appeals not because of the exercise of discretion by said Board but because the Board refused, failed and did not exercise its discretion. The Board of Immigration Appeals is the body duly authorized, empowered and delegated by the Attorney General of the United States to exercise [12] the power to suspend deportation and to authorize voluntary departure under the Immigration and Nationality Act, 1952.

Accordingly plaintiff has exhausted his administrative remedies. Plaintiff has been permitted to remain out of custody, on bond.

(7) On or about February 9, 1956, plaintiff received by Certified Mail from the office of defendant a written notice that arrangements to effect the deportation of plaintiff pursuant to the aforesaid order of deportation were being made.

(8) Plaintiff's only entry into the United States was at Rouses Point, New York, on March 18, 1947, on a valid visa as a temporary visitor for pleasure for a period of two weeks. An extension of that visa has neither been applied for nor granted.

### Issues of Law

1. Is the holding by the Board of Immigration Appeals that plaintiff failed to furnish address information as required by Section 265 of the Immigration and Nationality Act (8 USC 1305) based upon reasonable, substantial and probative evidence?

2. If the answer to Issue No. 1 is yes, is the holding of the Board of Immigration Appeals that such failure was not reasonably excusable or was not wilful, based upon reasonable, substantial and probative evidence?

3. Is the holding of the Board of Immigration Appeals that plaintiff is deportable under Section 241 (a) (5) of the Immigration and Nationality Act (8 USC 1251 (a) (5)), arbitrary or capricious?

### Issues of Law

1. Is plaintiff entitled to have the question of his eligibility for suspension of deportation con-

sidered under Section 244 (a) (1) of the Immigration and Nationality Act (8 USC 1254 (a) (1))?

2. Is plaintiff eligible for voluntary departure under Section 244 (e) of the Immigration and Nationality Act (8 USC 1254 (e))?

The foregoing admissions of fact have been made by the parties [13] in open court at the pretrial conference; and issues of fact and law being thereupon stated and agreed to, the Court makes this Order which shall govern the course of the trial unless modified to prevent manifest injustice.

Dated Nov. 26, 1956.

/s/ WM. M. BYRNE,  
Judge of U. S. District Court.

The foregoing pretrial Order is hereby approved:

/s/ FRED OKRAND,  
Attorney for Plaintiff.

/s/ VOLNEY V. BROWN, JR.,  
Attorney for Defendant.

[Endorsed]: Filed November 26, 1956. [14]

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[Title of District Court and Cause.]

### MEMORANDUM OF DECISION

Bennie Sevitt is an alien, a native and citizen of Ireland who entered the United States on March 18, 1947, with a visitor's visa. He has resided in this country continuously since that time.

After a hearing conducted by a Special Inquiry Officer of the Immigration and Naturalization Service, Sevitt was found to be deportable under 8 U.S.C. 1251 (a) (5)<sup>1</sup> for failure to register and notify the Immigration and Naturalization Service of his address in the United States or to notify them of changes of address as required by 8 U.S.C. 1305. Timely application for suspension of deportation was filed and an appeal was taken to the Board of Immigration Appeals, which Board dismissed the appeal and refused to consider plaintiff's application for suspension of deportation because it thought it was barred from doing so. [15]

Sevitt has exhausted his administrative remedies and here seeks judicial review of the administrative action. 5 U.S.C. 1009; 8 U.S.C. 1252; *Shaughnessy v. Pedreiro*, 349 U.S. 48.

The plaintiff asserts that there is no reasonable, substantial or probative evidence to support the administrative finding that he failed to furnish address information as required by 8 U.S.C. 1305, or to support the finding that such failure was wilful

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<sup>1</sup>Plaintiff was also found deportable for violation of 8 U.S.C. 1251 (a)(9), in that as a temporary visitor for pleasure he failed to comply with the conditions of that status. However, in this proceeding we are only concerned with the administrative decision relating to 8 U.S.C. 1251(a)(5), as the ultimate issue here is whether the plaintiff's application for suspension of deportation may be considered, and the determination of that issue depends upon the construction to be given 8 U.S.C. 1251 (a)(5).

and not excusable. This argument is without merit. The administrative record shows (Brief filed with Board) Sevitt conceded “\* \* \* that until the time of his arrest by Immigration Officers he did not furnish the required address information” and that “he failed to register because he feared detection \* \* \*” The record also shows that during the period he failed to comply with the address requirements, he used a fictitious name. It is an understatement to say that the administrative findings were based upon reasonable, substantial and probative evidence.

A more serious problem is presented on the question of whether the Board of Immigration Appeals erred in refusing to consider Sevitt’s application for suspension of deportation.

The authority to grant the relief of suspension of deportation is found in 8 U.S.C. 1254(a)<sup>2</sup> which is divided into five paragraphs numbered (1) to (5).

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<sup>2</sup>§ 1254 Suspension of Deportation—Adjustment of status for permanent residence; contents:

(a) As hereinafter prescribed in this section, the Attorney General may, in his discretion, suspend deportation and adjust the status to that of an alien lawfully admitted for permanent residence, in the case of an alien who:

(1) Applies to the Attorney General within five years after the effective date of this chapter for suspension of deportation; last entered the United States more than two years prior to June 27, 1952; is deportable under any law of the United States and is not a member of a class of aliens whose deportation could not have been suspended by reason of section 19(d) of the Immigration Act of 1917,



Each of the five [16] paragraphs relates to different classes of aliens, the classification depending upon when the alien entered the United States, the grounds of deportation, whether the deportable act

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as amended; and has been physically present in the United States for a continuous period of not less than seven years immediately preceding the date of such application, and proves that during all of such period he was and is a person of good moral character; and is a person whose deportation would, in the opinion of the Attorney General, result in exceptional and extremely unusual hardship to the alien or to his spouse, parent or child, who is a citizen or an alien lawfully admitted for permanent residence; or

(2) Last entered the United States within two years prior to or at any time after June 27, 1952; is deportable under any law of the United States solely for an act committed or status existing prior to or at the time of such entry into the United States and is not within the provisions of paragraph (4) of this subsection; was possessed of all of the requisite documents at the time of such entry into the United States; has been physically present in the United States for a continuous period of not less than five years immediately preceding his application under this paragraph, and proves that during all of such period he has been and is a person of good moral character; has not been served with a final order of deportation issued pursuant to this chapter in deportation proceedings up to the time of applying to the Attorney General for suspension of deportation; and is a person whose deportation would, in the opinion of the Attorney General, result in exceptional and extremely unusual hardship to the alien or to his spouse, parent or child, who is a citizen or an alien lawfully admitted for permanent residence; or

(3) Last entered the United States within two years prior to, or at any time after June 27, 1952;

was committed or status existed prior to entry, at the time of entry, or subsequent to entry, and the length of time the alien has been present in the United States.

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is deportable under any law of the United States for an act committed or status acquired subsequent to such entry into the United States and is not within the provisions of paragraphs (4) or (5) of this subsection; as possessed of all of the requisite documents at the time of such entry into the United States; has been physically present in the United States for a continuous period of not less than five years immediately following the commission of an act, or the assumption of a status, constituting a ground for deportation, and proves that during all of such period he has been and is a person of good moral character; has not been served with a final order of deportation issued pursuant to this chapter in deportation proceedings up to the time of applying to the Attorney General for suspension of deportation; and is a person whose deportation would, in the opinion of the Attorney General, result in exceptional and extremely unusual hardship to the alien or to his spouse, parent, or child, who is a citizen or an alien lawfully admitted for permanent residence; or

(4) Last entered the United States within two years prior to, or at any time after June 27, 1952; is deportable under paragraph (1) of section 1251 (a) of this title insofar as it relates to criminals, prostitutes or other immoral persons, subversives, violators of narcotic laws and similar classes or under paragraph (2) of section 1251 (a) of this title, as a person who entered the United States without inspection or at a time or place other than as designated by the Attorney General, or without the proper documents and is not within the provisions of paragraph (5) of this subsection; has been physically present in the United States for a continuous period of not less than ten years after such entry and immediately preceding his application

The complexity of the problem in the instant case results from the fact that an alien such as Sevitt who has violated the registration requirements falls

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under this paragraph and proves that during all of such period he has been and is a person of good moral character; has not been served with a final order of deportation issued pursuant to this chapter in deportation proceedings up to the time of applying to the Attorney General for suspension of deportation; and is a person whose deportation would, in the opinion of the Attorney General, result in exceptional and extremely unusual hardship to the alien or to his spouse, parent, or child, who is a citizen or an alien lawfully admitted for permanent residence; or

(5) Is deportable under paragraphs (4)-(7), (11), (12), (14-17), or (18) of section 1251(a) of this title for an act committed or status acquired subsequent to such entry into the United States or having last entered the United States within two years prior to, or at any time after June 27, 1952, is deportable under paragraph (2) of section 1251 (a) of this title as a person who has remained longer in the United States than the period for which he was admitted; has been physically present in the United States for a continuous period of not less than ten years immediately following the commission of an act, or the assumption of a status, constituting a ground for deportation, and proves that during all of such period he has been and is a person of good moral character; has not been served with a final order of deportation issued pursuant to this chapter in deportation proceedings up to the time of applying to the Attorney General for suspension of deportation; and is a person whose deportation would, in the opinion of the Attorney General, result in exceptional and extremely unusual hardship to the alien or to his spouse, parent, or child, who is a citizen or an alien admitted for permanent residence.

within the provisions of both paragraph (1) and paragraph (5), except that to be eligible for suspension of deportation under (5), the alien must have been physically present in the United States for a continuous period of not less than ten years immediately [17] following the commission of the act (failure to register) for which he is deportable; whereas to be eligible under (1), the alien need only be present in the United States for a period of not less than seven years immediately preceding the date of application for suspension of deportation. The crucial importance of this difference to Sevitt is that he has been in this country for the seven-year period required under (1) but has not been in the country for the ten-year period required under (5).

The Board of Immigration Appeals refused to consider Sevitt's application for suspension of deportation for the reason, as counsel for the Government now argues, that while the reference in paragraph (1) to aliens "deportable under any law of the United States" technically includes aliens deportable for failure to meet registration requirements, paragraph (1) does not apply to such aliens because paragraph (5) specifically refers to the section of law making that offense deportable. It is the government's position that when an alien is deportable under any provision of law specifically mentioned in paragraph (5), his application for suspension of deportation may be considered, if at all, only under that paragraph.

The five paragraphs of § 1254(a) show a statutory design to enact remedial legislation covering a number of different contingencies. In formulating the several possible categories, Congress provided that a deportable alien is eligible for the discretionary relief of suspension of deportation if he qualifies under the provisions of paragraphs (1) or (2) or (3) or (4) or (5). By the use of the disjunctive conjunction, "or," it is clear that Congress intended to present a choice dependent only upon the alien meeting the standards as required [19] in the particular paragraph he seeks to avail himself of. Sevitt satisfies the requirements of paragraph (1) as he applied for the relief within five years after the effective date of the 1952 Act; he entered the United States more than two years prior to the enactment of the Act; he is deportable under a law of the United States and is not a member of a class of aliens whose deportation could not have been suspended by reason of section 19(d) of the 1917 Act; he has been physically present in the United States for a continuous period of not less than seven years immediately preceding the date of his application. It follows that his application should have been considered by the Board of Immigration Appeals.

Under the provisions of § 1254(e) an alien who is deportable for failure to comply with the registration requirements may be granted the privilege of voluntary departure only if he can meet the ten-year requirement of § 1254(a)(5). It is unreasonable to believe, asserts the government, that notwith-

standing Sevitt's inability to meet the standards for the discretionary relief of voluntary departure, Congress intended that he be eligible for the greater relief of suspension of deportation under the standards set forth in paragraph (1) of § 1254(a). The answer to this assertion may be found [20] in the time limitation of paragraph (1) which paragraph by its terms becomes ineffective after June 27, 1957. However, be that as it may, the courts should not resort to conjecture regarding policy decisions of Congress.

While it is the rule that the courts may depart from the strict wording of a statute in order to give the statute a reasonable construction where a literal construction would result in an absurdity or defeat the object intended by Congress (*Miller v. Bank of America, N. T. & S. A.* (CA 9), 166 F. 2d 415), where the statute is clear and unambiguous it must be literally construed. *Hamilton v. Rathbone*, 175 U.S. 414; *Thompson v. United States*, 246 U.S. 547; *Crooks v. Harrelson*, 282 U.S. 55. Nothing could be clearer than the statement of Congress that the Attorney General may, in his discretion, suspend deportation in the case of an alien who meets the standards prescribed in paragraph (1) of § 1254 (a).

This Court in *Acosta v. Landon*, 125 F. Supp. 434, 441, said:

“The courts may not suspend the deportation of a deportable alien as that discretionary

power is vested solely in the Attorney General, 8 U.S.C.A., § 1254. However, when the Attorney General is required as a condition precedent to an order of deportation to exercise his discretion with respect to the suspension of deportation, the validity of the order must rest upon the needed exercise of discretion. If it is lacking the order is ineffective. Where the order is ineffective, the custody of the petitioner is unlawful, and the court must order his discharge. A formal order to that effect will be entered."

*Acosta v. Landon* was a habeas corpus proceeding and *Acosta* was in custody. *Sevitt* is not in custody and there is no need to order his discharge. However, the order of deportation is ineffective and the alien may not be deported until the Attorney General, acting through his subordinates, has exercised his discretion. Judgment will be entered accordingly.

Counsel for plaintiff will prepare, serve and lodge findings and judgment pursuant to Rule 7 of the Rules of this Court.

Dated March 26, 1957.

/s/ WM. M. BYRNE,

United States District Judge.

[Endorsed]: Filed March 27, 1957. [21]

In the United States District Court, Southern  
District of California, Central Division

No. 19588—WB

BENNIE SEVITT,

Plaintiff,

vs.

ALBERT DEL GUERCIO, Officer in Charge, Im-  
migration and Naturalization Service, Los An-  
geles, California,

Defendant.

### FINDINGS OF FACT, CONCLUSIONS OF LAW AND JUDGMENT

The above-entitled cause came on regularly for trial on January 21, 1957, in the above-entitled court before the Honorable William M. Byrne, Judge, presiding without a jury; the plaintiff was represented by his attorneys, Wirin, Rissman & Okrand, by Fred Okrand; the defendant was represented by his attorneys, Laughlin E. Waters, United States Attorney; Max F. Deutz and Volney V. Brown, Jr., Assistants United States Attorney, by Volney V. Brown, Jr. Evidence having been introduced on behalf of the plaintiff and the defendant, and the court having considered same, and the court having heard the arguments of counsel and being fully advised in the premises, now makes the following: [22]



Findings of Fact

I.

Plaintiff, Bennie Sevitt, is a resident of Los Angeles, California. He is a native and citizen of Ireland. He is thirty-seven years old.

II.

Defendant, Albert Del Guercio, is the duly appointed and acting Officer in Charge of the Immigration and Naturalization Service, United States Department of Justice, for the Los Angeles area. Defendant is charged with the administration and enforcement of the immigration and naturalization laws of the United States within said area and within the Southern District of California.

III.

On or about March 24, 1954, plaintiff was served with a Warrant of Arrest and charged with being subject to deportation under 8 USC 1251(a)(9) as an alien who, after his legal admission into the United States as a visitor for pleasure, failed to comply with the conditions of such status.

IV.

Subsequent to said arrest, hearings were held. During the course of said hearings an additional charge was lodged to the effect that plaintiff was subject to deportation under 8 USC 1251(a)(5) as an alien who failed to furnish address information as required by Section 265 of the Immigration and Nationality Act (8 USC 1305).

On or about December 8, 1955, a Special Inquiry Officer of the Immigration and Naturalization Service determined that plaintiff was subject to deportation on both grounds and entered an order that plaintiff be deported.

Appeal from said decision and order was taken to the Board of Immigration Appeals, which Board, on or about January 24, 1956 [23] dismissed the appeal, as a consequence of which said Order of Deportation became final.

#### V.

During said proceedings plaintiff filed timely applications for suspension of deportation and/or voluntary departure. Said applications were denied by the Board of Immigration Appeals not because of the exercise of discretion by said Board but because the Board refused, failed and did not exercise its discretion, under 8 USC 1254(a)(1) because it thought it was barred from doing so. The Board of Immigration Appeals is the body duly authorized, empowered and delegated by the Attorney General of the United States to exercise the power to suspend deportation and to authorize voluntary departure under the Immigration and Nationality Act, 1952.

Accordingly plaintiff has exhausted his administrative remedies. Plaintiff has been permitted to remain out of custody, on bond.

#### VI.

On or about February 9, 1956, plaintiff received by Certified Mail from the office of defendant a

written notice that arrangements to effect the deportation of plaintiff pursuant to the aforesaid order of deportation were being made.

## VII.

Plaintiff's only entry into the United States was at Rouses Point, New York, on March 18, 1947, on a valid visa as a temporary visitor for pleasure for a period of two weeks. An extension of that visa has neither been applied for nor granted. Plaintiff has resided in this country continuously since that time.

## VIII.

The administrative record shows that until the time of his [24] arrest by Immigration Officers, Plaintiff did not furnish the required address information and he did not register as an alien because he feared detection.

From the foregoing Findings of Fact, the court makes the following:

## Conclusions of Law

### I.

This court has jurisdiction by virtue of the Administrative Procedures Act (5 USC 1001-1011), particularly Section 10 thereof (5 USC 1009), by virtue of Section 242 (3) of the Immigration and Nationality Act, 1952 (8 USC 1252 (e)), and by virtue of the Declaratory Judgments Act (28 USC 2201, et seq.), to declare said Order and Warrant unlawful, illegal and void, to vacate said Order and

Warrant and terminate the within deportation proceeding and to restrain and enjoin defendant and his agents from executing or otherwise acting upon an unlawful and illegal Order and Warrant of Deportation.

## II.

The holding by the Board of Immigration Appeals that plaintiff is deportable under 8 USC 1251(a)(5) is based upon reasonable, substantial and probative evidence.

## III.

The Board of Immigration Appeals erred in refusing to consider plaintiff's application for suspension of deportation under 8 USC 1254(a)(1).

## IV.

The order of deportation is ineffective and plaintiff may not be deported unless and until the Attorney General, acting through his subordinates, exercises his discretion. [25]

## V.

Let judgment be entered accordingly.

## Judgment

In accordance with the foregoing Findings of Fact and Conclusions of Law,

It Is Ordered, Adjudged and Decreed:

1. The Order of Deportation of December 8, 1955, by the Special Inquiry Officer, as affirmed by

the Order of the Board of Immigration Appeals of January 24, 1956, that plaintiff, Bennie Sevitt, be deported is ineffective.

2. Plaintiff, Bennie Sevitt, may not be deported unless, or until, the Attorney General, acting through his subordinates, has exercised his discretion as to whether said Bennie Sevitt shall be granted suspension of deportation.

Dated: April 2, 1957.

/s/ WM. M. BYRNE,  
Judge, U. S. District Court.

Approved as to form in accordance with Local Rule 7, this .... day of ....., 1957.

/s/ BRUCE A. BEVAN, JR.,  
Assistant United States  
Attorney.

[Endorsed]: Filed April 2, 1957.

Docketed and entered April 3, 1957. [26]

---

[Title of District Court and Cause.]

NOTICE OF APPEAL

[Rule 73b F.R.C.P.]

Defendant hereby appeals to the United States Court of Appeals for the Ninth Circuit from the Judgment entered in this action by the above-entitled Court on April 2, 1957.

Dated: May 31, 1957.

LAUGHLIN E. WATERS,  
United States Attorney;

RICHARD A. LAVINE,  
Assistant U. S. Attorney,  
Chief of Civil Division;

/s/ BRUCE A. BEVAN, JR.,  
Assistant U. S. Attorney,  
Attorneys for Defendant.

Affidavit of Service by Mail attached.

[Endorsed]: Filed May 31, 1957. [27]

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[Title of District Court and Cause.]

### CERTIFICATE BY CLERK

I, John A. Childress, Clerk of the above-entitled Court, hereby certify that the items listed below constitute the transcript of record on appeal to the United States Court of Appeals for the Ninth Circuit, in the above-entitled case:

A. The foregoing pages, numbered 1 to 33, inclusive, containing the original

Complaint;

Answer;

Pretrial Order;

Memorandum of Decision;

Findings of Fact, Conclusions of Law and  
Judgment;

Notice of Appeal;

Appellant's Designation of Record on Appeal;

Motion to Extend Time for Filing and Docketing Record on Appeal;

B. Defendant's Exhibit A.

I further certify that the fee for preparing the foregoing record, amounting to \$1.60 has not been paid by appellant.

Witness my hand and seal of the said District Court this 24th day of July, 1957.

[Seal]                      JOHN A. CHILDRESS,  
Clerk;

By /s/ WM. A. WHITE,  
Deputy Clerk.

---

[Endorsed]: No. 15642. United States Court of Appeals for the Ninth Circuit. Albert Del Guercio, Officer in Charge, Immigration and Naturalization Service, Los Angeles, Calif., Appellant, vs. Bennie Sevitt, Appellee. Transcript of Record. Appeal from the United States District Court for the Southern District of California, Central Division.

Filed July 25, 1957.

/s/ PAUL P. O'BRIEN,  
Clerk of the United States Court of Appeals for the Ninth Circuit.

United States Court of Appeals  
for the Ninth Circuit

No. 15642

ALBERT DEL GUERCIO, Officer in Charge, Im-  
migration and Naturalization Service, Los An-  
geles, California,

Appellant,

vs.

BENNIE SEVITT,

Appellee.

APPELLANT'S STATEMENT OF POINTS

Pursuant to Rule 17(6) of this Court, appellant relies upon the following statement of points:

1. The trial court erred in adjudging that appellee may not be deported until his application for suspension of deportation has been considered under 8 U.S.C., § 1254(a)(1).

2. The trial court erred in concluding that the Board of Immigration Appeals erred in refusing to consider appellee's application for suspension of deportation under 8 U.S.C., § 1254(a)(1).

3. The trial court erred in deciding that appellee's application for suspension of deportation should have been considered under 8 U.S.C., § 1254(a)(1).

4. The trial court erred in deciding that appellee's application for suspension of deportation



should not have been considered under 8 U.S.C., § 1254(a)(5).

Dated: This 21st day of August, 1957.

LAUGHLIN E. WATERS,  
United States Attorney;

RICHARD A. LAVINE,  
Assistant U. S. Attorney,  
Chief of Civil Division;

/s/ BRUCE A. BEVAN, JR.,  
Assistant U. S. Attorney,  
Attorneys for Appellant.

[Endorsed]: Filed August 23, 1957.

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[Title of Court of Appeals and Cause.]

STIPULATION FOR CONSIDERATION OF  
EXHIBIT IN ITS ORIGINAL FORM

It Is Hereby Stipulated by and between the parties hereto, through their respective counsel and subject to the approval of this Court, that defendant's Exhibit A (the certified copy of administrative proceedings) may be considered in its original form by this Court in connection with the pending appeal, and need not be printed.

Dated: This 21st day of August, 1957.

LAUGHLIN E. WATERS,  
United States Attorney;

RICHARD A. LAVINE,  
Assistant U. S. Attorney,  
Chief of Civil Division;

/s/ BRUCE A. BEVAN, JR.,  
Assistant U. S. Attorney,  
Attorneys for Appellant.

WIRIN, RISSMAN & OKRAND,

By /s/ FRED OKRAND,  
Attorneys for Appellee.

So Ordered:

/s/ STEPHENS,  
Chief Judge, U. S. Court of Appeals for the Ninth  
Circuit.

[Endorsed]: Filed August 29, 1957.

No. 15642.  
IN THE  
**United States Court of Appeals**  
FOR THE NINTH CIRCUIT

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ALBERT DEL GUERCIO, Officer in Charge, Immigration  
and Naturalization Service, Los Angeles, California,  
*Appellant,*

*vs.*

BENNIE SEVITT,

*Appellee.*

---

**APPELLANT'S OPENING BRIEF.**

---

LAUGHLIN E. WATERS,  
*U. S. Attorney,*

RICHARD A. LAVINE,  
*Assistant U. S. Attorney,*  
*Chief, Civil Division,*

BRUCE A. BEVAN, JR.,  
*Assistant U. S. Attorney,*  
600 Federal Building,  
Los Angeles 12, California,  
*Attorneys for Appellant.*

**FILED**

OCT 17 1957

PAUL P O BRIEN, CLERK

THE HISTORY OF THE CITY OF BOSTON

FROM 1630 TO 1830

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United States Code, Title 8, Sec. 1254(a) (2).....	5, 6, 19, 20
United States Code, Title 8, Sec. 1254(a) (3) .....	5, 20, 21
United States Code, Title 8, Sec. 1254(a) (4).....	5, 6, 19, 20
United States Code, Title 8, Sec. 1254(a) (5).....	
.....	5, 6, 7, 10, 13, 14, 16, 18, 19, 20, 21
United States Code, Title 8, Sec. 1254(e).....	20
United States Code, Title 8, Sec. 1305.....	1, 5, 7, 10, 12, 14, 17
United States Code, Title 8, Sec. 1306(b).....	5, 12, 13
United States Code, Title 8, Sec. 1329.....	2
United States Code, Title 18, Secs. 9-13.....	11
United States Code, Title 28, Sec. 1291.....	2
United States Code, Title 28, Sec. 2201.....	2





No. 15642.

IN THE

# United States Court of Appeals

FOR THE NINTH CIRCUIT

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ALBERT DEL GUERCIO, Officer in Charge, Immigration  
and Naturalization Service, Los Angeles, California,  
*Appellant,*

*vs.*

BENNIE SEVITT,

*Appellee.*

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## APPELLANT'S OPENING BRIEF.

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### Statement of Jurisdiction.

Or or about March 24, 1954, appellee was served with a Warrant of Arrest which charged that he was subject to deportation under 8 United States Code §1251(a)(9), as an alien who, after his admission into the United States at Rouses Point, New York, on March 18, 1947, as a temporary visitor for pleasure, failed to comply with the conditions of such status. [T. R. 11, 13.]<sup>1</sup>

Subsequent to the arrest, deportation proceedings were conducted during the course of which an additional charge was lodged to the effect that appellee was subject to deportation under 8 United States Code §1251(a)(5), as an alien who had failed to furnish address information as required by the Alien Registration Act (8 United States Code, §1305). [T. R. 11-12.] On or about

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<sup>1</sup>T. R. refers to the Clerk's Transcript of Record.

December 8, 1955, a Special Inquiry Officer determined that appellee was subject to deportation on both grounds and entered an order of deportation accordingly. [T. R. 12.]

An administrative appeal from said decision and order was taken to the Board of Immigration Appeals. (*Ibid.*) Appellee filed a timely application for suspension of deportation under 8 United States Code §1254(a)(1), which was denied by said Board on the ground that appellee was not eligible for such relief. (*Ibid.*) On January 24, 1956, the Board affirmed the decision and order of the Special Inquiry Officer by dismissing the appeal. (*Ibid.*)

A Complaint for Injunction and Declaratory Judgment was filed in the District Court for the Southern District of California at Los Angeles on March 2, 1956. [T. R. 3-8.] Appellant's Answer was filed on April 19, 1956. [T. R. 9-10.] The case was tried on January 21, 1957, by the Honorable William M. Byrne, District Judge, who rendered a decision on March 26, 1957 (reported at 150 Fed. Supp. 56). [T. R. 14-23.] Judgment was entered on April 2, 1957, in favor of appellee. [T. R. 24-29.] Appellant filed a timely notice of appeal on May 31, 1957. [T. R. 29-30.]

The District Court had jurisdiction of the action under 8 United States Code §1329, 5 United States Code §1009, and 28 United States Code §2201, *et seq.*

This Court has jurisdiction of the appeal under 28 United States Code §1291.

### Statement of the Case.

The decision and judgment of the District Court determined that the holding by the Board of Immigration Appeals that appellee is deportable under 8 United States Code §1251(a)(5), was based upon reasonable, substantial and probative evidence. Such conclusion, of course, we do not question.

The District Court also determined, however, that the administrative agency should have considered appellee's application for suspension of deportation under 8 United States Code §1254(a)(1). The correctness of this ruling is the only question raised on appeal.

### Specification of Errors.

1. The District Court erred in adjudging that appellee may not be deported until his application for suspension of deportation has been considered under 8 United States Code §1254(a)(1). [T. R. 29.]

2. The District Court erred in concluding that the Board of Immigration Appeals erred in refusing to consider appellee's application for suspension under 8 United States Code §1254(a)(1). [T. R. 28.]

3. The District Court erred in deciding that appellee's application for suspension of deportation should have been considered under 8 United States Code §1254(a)(1). [T. R. 21.]

### Summary of Argument.

Suspension of deportation is available under the Immigration and Nationality Act of 1952 in 8 United States Code §1254(a)(1), (2), (3), (4), and (5), the applicability of the five paragraphs being dependent upon the grounds of deportation, the time of entry, period of residence within the United States and other factors. Although paragraph (5) specifically applies to the ground of Mr. Sevitt's deportation, such ground is not specifically excluded from the application of the more general provisions of paragraph (1). Thus statutory construction is necessary to resolve the question of which paragraph, if not both, is applicable to appellee.

Our argument is that it was the intent of the 1952 Congress in enacting 8 U. S. C. §1254(a)(5), to severely limit the relief of suspension of deportation for the offenses designated therein, and to effectuate this intention, paragraph (5) should be construed as being the only paragraph of §1254(a) which governs applications for suspension of such offenses. Our argument is based upon the following major points:

1. The offense which renders appellee deportable, a violation of §1305, was not a ground of deportation until passage of the 1952 Act. Under this Act, a violation subjects one to deportation under 8 U. S. C. §1251(a)(5) even though the alien is not convicted for the offense. (8 U. S. C. §1306(b).) Therefore, the 1952 Congress indicated a sternness towards such offenses.

2. A further such indication is the fact that deportations under §1251(a)(5) are specifically included in the suspension provisions of §1254(a)(5) in which the most serious grounds of deportation are enumerated. The suspension relief in paragraph (5) for major violations is much more rigid than for the minor offenses suspendable under paragraphs (1), (2), and (3). Presumably, therefore, Congress would not intend the more liberal relief provisions of paragraph (1) to apply to what it considers a major violation.

3. Moreover, relief under §1254(a)(1) specifically is not available to persons ineligible for such relief under §19(d) of the 1917 Act, as amended. (8 U. S. C. §155(d).) Such previously ineligible offenses are the same major offenses now eligible for suspension under the strict standards of §1254(a)(5). Consequently, the exclusion from paragraph (1) of a class into which appellee specifically is included would seem to show clearly Congressional intention to exclude appellee's class from paragraph (1).

4. Relief under paragraph (1) was intended only for persons eligible therefor under former 8 United States Code, §155(c). Appellee could not have been intended to come within the scope of paragraph (1) since he was not eligible for relief under the former Act, due to the fact that he was not subject to deportation until the 1952 Act.

5. Relief under paragraph (1) was intended to exist only for a limited time, and expires on December 31,

1957. Congress could not have intended appellee to be within the scope of (1), since he is specifically eligible for an unlimited period of relief under paragraph (5) of §1254(a).

6. A normal rule of statutory construction is that provisions specifically treating a certain subject matter control general provisions which also may include that subject matter. Under this rule, only §1254(a)(5), which specifically treats the ground of appellee's deportation, can govern the application for suspension, even though the literal terms of §1254(a)(1) could also so govern.

7. If §1305 offenses are suspendable under paragraph (1), certain absurd results occur which Congress presumably never would have intended. An adequate explanation of these absurdities would require more space than a summary permits, so the details thereof are left to the body of the Argument.

## ARGUMENT.

### I.

#### Preliminary Statement.

The question involved in this appeal is one solely of statutory construction.<sup>2</sup> The literal terms both of 8 U. S. C. §1254(a)(1) and of 8 U. S. C. §1254(a)(5) can govern the application of appellee for suspension of deportation. [T. R. 19-20.] The difference to Mr. Sevitt is that he has met the seven year physical presence requirement of paragraph (1) but not the ten year requirement of paragraph (5); thus the Immigration Service can consider the application if (1) is applicable, but cannot if (5) is applicable.

The trial court concluded that Congress intended to give aliens a choice of the five paragraphs of §1254(a) under which to file their applications for suspension, dependent only upon the aliens qualifying under the literal standards of each paragraph. [T. R. 21.] It is our position that Congress intended only paragraph (5) to apply to aliens who, as has Mr. Sevitt, violated the Alien Registration Act. Our argument to a large extent will be based upon *Dessalernos v. Savoretti*, 244 F. 2d 178 (C. A. 5, 1957), decided since the District Court opinion. The *Dessalernos* case is on all fours, and since the Fifth Circuit so keenly analyzed the statutory problem involved herein, we must apologize in advance for adopting so much of that Court's reasoning.

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<sup>2</sup>The pertinent statutes are set forth in the Appendix.



II.

**Construction of the Statute Is Necessary.**

The trial court rejected arguments based upon statutory construction of §1254(a) on the ground that “the statute is clear and unambiguous.” [T. R. 22.] We agree that construction normally should not occur where there is no ambiguity in a statute.

“ . . . the province of construction lies wholly within the domain of ambiguity . . . ”

*Hamilton v. Rathbone*, 175 U. S. 414, 421 (1899).

“The intention of the Congress is to be sought for primarily in the language used, and where this expresses an intention reasonably intelligible and plain it must be accepted without modification by resort to construction or conjecture.”

*Thompson v. United States*, 246 U. S. 547, 551 (1918).

“The principle that a clear and unambiguous statute must be literally construed is long established.”

*Miller v. Bank of America*, 166 F. 2d 415, 417 (9 Cir., 1948).

We also agree with the lower court’s statement that 8 U. S. C. §1254(a)(1) is plain and clear in its terms. We respectfully submit, however, that a question of whether one portion of a statute is in conflict with another cannot be resolved by confining scrutiny to one such portion. Otherwise, there never would have been the necessity for the familiar rule that “where there is inconsistency between general and special provisions of an act, the latter control.”

*United States v. Mattio*, 17 F. 2d 879 (9 Cir., 1927).

The correct method of determining whether statutory construction of §1254(a) is necessary would require a reading of its paragraph (1) together with paragraph (5); then if no ambiguity is present, construction is unnecessary. Under such a test, the ambiguity of the section is manifest.

The five paragraphs of §1254(a) are mutually exclusive except with respect to grounds of deportability arising under paragraphs (5) and (17) of §1251(a). (*Dessalernos v. Savoretti*, 244 F. 2d, *supra*, p. 183.) Appellee is deportable under §1251(a)(5) to which §1254(a)(5) expressly is applicable. Appellee is also, therefore, "deportable under any law of the United States" within the meaning of §1254(a)(1). The offense which makes him deportable, a violation of 8 United States Code, §1305, in that he failed to provide changes of address as required by the Alien Registration Act, was not a ground of deportation under the pre-1952 law. Thus such offense is not within the express exclusion of §1254(a)(1), namely, appellee "is not a member of a class of aliens whose deportation could not have been suspended by reason of section 19(d) of the Immigration Act of 1917, as amended."

Consequently, paragraph (5) of §1254(a) is expressly applicable to the ground of appellee's deportation, and paragraph (1) does not expressly exclude such ground. The problem of resolving the two paragraphs with respect to §1251(a)(5) offenses immediately arises: Do both paragraphs apply to such offenses? If only one applies, which one? It is very apparent that §1254(a)(1) does not plainly and unambiguously apply to the aliens in Mr. Sevitt's class when read in conjunction with §1254(a)(5). Therefore, it is necessary to resort to

the principles of construction to determine which paragraph, if not both, Congress intended to be applicable to violations of the Alien Registration Act.

### III.

#### History and Purpose of the 1952 Changes in the Immigration Law.

The 1952 Immigration and Nationality Act completely revised the former provisions of law relating to the Alien Registration Act and to suspension of deportation. Since it was such revision which resulted in the ambiguity this Court is called upon to resolve, it is essential that we discover what changes were made and why. Such an inquiry into legislation history and purpose is proper, as was held in *Acheson v. Fujiko Furusho*, 212 F. 2d 284 (C. A. 9, 1954):

“In the early case of *Smythe v. Fiske*, 1874, 90 U. S. 374, 380, 23 L. Ed. 47, it is said, ‘Where doubt exists as to the meaning of a statute, \* \* \* [t]he pre-existing law, and the reason and purpose of the new enactment are also considerations of great weight.’”

The appropriate starting point of inquiry into the legislative history of the 1952 Act is the Alien Registration Act of 1940, found at c. 439, 54 Stat. 670-676. Title I of the Act, dealing with subversive activity, was codified in former 18 United States Code §§9-13. Title II, concerning deportation and suspension of deportation, was codified in 8 United States Code §155(b), (c) and (d). Title III, pertaining to the requirements and procedures of registration, was codified in 8 United States Code §§451-460.

The provisions of Title II and III are what concern Mr. Sevitt. The crucial ground of his order of deportation is his failure to provide the Attorney General with a change of address. [T. R. 15.] Prior to 1952, his duty to do so arose under 8 United States Code §456. The only penalty for failure to comply was set forth in 8 U. S. C. §457(b), which provided a maximum punishment of \$100 fine and/or 30 days imprisonment. The 1952 Act sets forth his duty in 8 U. S. C. §1305, and the penalty in §1306(b). Although the duty and penalty provisions were retained in substance, a very striking *addition* to the penalty was made; even though an alien was not convicted of a violation of §1305, the 1952 Act made him subject to deportation for failure to comply unless the alien could prove that his failure was not wilful. It is thus very much an understatement to say that Congress took a more severe view in 1952 of this type of violation.

Inasmuch as *Dessalernos v. Savoretti*, *supra*, p. 181-184, thoroughly reviews the antecedent history of laws governing the suspension of deportation and the 1952 changes therein, we shall merely summarize the developments in those laws. Suspension of deportation was not available under the pre-1952 law to aliens specified in 8 United States Code §155(d), *i. e.*, anarchists, narcotic offenders, criminals, immoral persons, etc. As to aliens who were eligible for such relief under the old law, the present 8 U. S. C. §1254(a)(1) authorizes the continuance thereof until December 31, 1957, for aliens who had entered prior to June 27, 1950. Section 1254(a)(1) expressly excludes from its application those aliens who were ineligible under the old law.

Section 1254(a)(5) authorizes suspension of deportation to those aliens previously excluded therefrom under the pre-1952 law, but under severe limitations. If the application of §1254(a)(5) had been confined solely to aliens in §155(d), no conflict would exist between §1254(a)(1) and §1254(a)(5), at least with respect to the offense rendering appellee deportable. Instead, Congress enacted additional grounds of deportation in §1251(a)(17) and §1306(b), and specified that suspension of deportation for such offenses would be governed by §1254(a)(5). Consequently, conflict between §1254(a)(1) and §1254(a)(5) arises, because deportation under §1251(a)(17) and §1306(b) are “under any law of the United States” within the meaning of §1254(a)(1), and yet not specifically excluded therefrom because not mentioned, of course, in former §155(d).

#### IV.

#### Intent of Congress.

The fundamental principle of statutory construction is to give effect to the intention of the legislature.

“In every case of statutory interpretation, the aim is to discover the legislative intent.”

*Femmer v. City of Juneau*, 97 F. 2d 649, 656 (9 Cir., 1938).

“We invoke the principle so well stated in *Ozawa v. United States*, 1922, 260 U. S. 178, 194 . . . , as follows: ‘It is the duty of this Court to give effect to the intent of Congress. Primarily this intent is ascertained by giving the words their natural significance, but if this leads to an unreasonable result plainly at variance with the policy of the legislation as a whole, we must examine the matter further. We may then look to the reason of the enactment

and inquire into its antecedent history and give it effect in accordance with its design and purpose, sacrificing, if necessary, the literal meaning in order that the *purpose* may not fail . . .”

*Acheson v. Fujiko Furusho*, 212 F. 2d 284, 295 (C. A. 9, 1954).

The history and purpose of the pertinent changes in the 1952 law already have been seen, and provide such a clear picture of Congressional intention that the solving of the apparent ambiguity in §1254(a) becomes easy.

First, it has been seen that the 1952 Congress made violations of §1305 subject to the drastic penalty of deportation without the necessity of a conviction therefor. Next, this ground of deportation was included in §1254(a)(5) with the most serious such grounds, such as for anarchism, narcotic trafficking, prostitution, and other major criminal activity. These other serious offenses were excluded from the relief of suspension of deportation under the former §155(d). Finally, persons in the former ineligible classes under §155(d) are specifically excluded from relief in §1254(a)(1).

In view of the foregoing, it would seem incredible that Congress would have intended the easy relief available in paragraph (1) to apply to a new class specifically placed with the major offenses, when such major offenses were expressly excluded from paragraph (1) relief.

This conclusion is reinforced by remembering the purpose of paragraph (1) relief, which was to continue suspension of deportation for a limited period of minor offenders eligible for such relief under the former Act, provided their entry occurred before June 27, 1950. Congressional intention to “preserve” such relief for classes eligible therefor prior to the 1952 Act cannot

exist for appellee, since the ground of his deportation did not arise until 1952. Since he is not one of those aliens eligible for relief under the pre-1952 Act, he was not intended by Congress to be eligible under paragraph (1), which merely continues such relief.

Moreover, the cut-off date for relief under paragraph (1) gives a further clue as to the intent of the legislature. Since Congress desired to end suspension of deportation relief on December 31, 1957, to aliens in paragraph (1), obviously such paragraph did not include appellee, for he is eligible for such relief under paragraph (5), which has no time limitation. Thus the specific inclusion of appellee's category in paragraph (5) would seem to manifest Congressional intention to exclude the category from paragraph (1). This is merely another example of the soundness of the familiar principle that a specific provision prevails over a general provision. The Supreme Court, in *MacEvoy v. United States*, 322 U. S. 102, 107 (1944), stated the rule in the following strong language:

“However inclusive may be the general language of a statute, it ‘will not be held to apply to a matter specifically dealt with in another part of the same enactment . . . Specific terms prevail over the general . . .’”

The rule has been followed by this Court on many occasions. (*United States v. Mattio*, 17 F. 2d 879 (9 Cir. 1927); *Karrell v. United States*, 181 F. 2d 981, 986-7 (C. A. 9, 1950); *McLeod v. Nagle*, 48 F. 2d 189 (9 Cir. 1931).) In the *McLeod* case, former §155 was construed. There the contention was that even though the alien was in a class specifically made deportable, he likewise was in the general class of aliens who were excludable under the first, more general, provision of the section,

and his case should be dealt with under the less onerous conditions of the general provision. This Court stated that such an argument did not appeal to it, holding:

“‘It must be conceded that the appellee is a member of one of the classes excludable by law. \* \* \* But it must likewise be conceded that he also belongs to the special class for which no time limit is fixed, and under a familiar rule of statutory construction with special provision will control over the general one.’ \* \* \* Here Congress has expressly excepted aliens convicted of crime prior to their entry into the United States from the general classification of those who are excluded by law. The language is clear, and so to construe it gives each clause of section 19 its due importance \* \* \*”

We submit that the language of §155 interpreted in *McLeod* no more clearly excluded the special class from the general class there than does §1254(a) exclude the special class of paragraph (5) from the general class of paragraph (1). Therefore, the special provision of paragraph (5) should prevail over the general class of paragraph (1).

Of further significance is the mutual exclusivity of the five paragraphs of §1254(a). As noted by the *Dessalernos* opinion, 244 F. 2d, supra, pp. 183-184, the only breakdown in the mutual exclusivity of the section comes if deportations under §1251(a)(5) and (17) are held to come within §1254(a)(1) as well as §1254(a)(5). Under the construction urged by the Government, this overlap does not exist and the entire section is harmonious in that each paragraph is mutually exclusive. By such a construction, each paragraph is given its “due importance” as prescribed by *McLeod*.



V.

**The Statute Should Be Construed to Avoid Absurdities.**

Another principle of statutory construction which this Court has applied in the past is that enactments should be construed to avoid absurd results.

“‘. . . [S]tatutes should receive a sensible construction, such as will effectuate the legislative intention, and, if possible, so as to avoid an unjust or an absurd conclusion’ (Lau Ow Bew v. United States, 144 U. S. 47 . . .).”

*Haff v. Yung Poy*, 68 F. 2d 203 (9 Cir., 1933).

“We quote from *Sorrells v. United States*, 1932, 287 U. S. 435 . . . ‘Literal interpretation of statutes at the expense of the reason of the law and producing absurd consequences or flagrant injustice has frequently been condemned [citing cases]. \* \* \* ‘All laws should receive a sensible construction. *General terms should be so limited in their application as not to lead to injustice, oppression, or an absurd consequence.* It will always, therefore, be presumed that the legislature intended exceptions to its language which would avoid results of this character.’ . . .” (Emphasis added.)

*Acheson v. Fujiko Furusho*, 212 F. 2d 284, 295 (C. A. 9, 1954).

If 8 United States Code §1254(a)(1) governed appellee’s application for suspension of deportation, some rather absurd results occur.

A. As *Dessalernos v. Savoretti*, 244 F. 2d, supra, p. 184, pointed out, two aliens could violate 8 U. S. C. §1305 at precisely the same time and place, but the consequences

to them would be entirely different depending solely on the date of entry. For a violation in 1954, as occurred herein, the easier relief provisions of §1254(a)(1) are available to aliens entering before June 27, 1950, but not to those entering the United States after that date. Under some circumstances, there might be a reason behind leniency towards aliens entering earlier—but here there would appear to be none, since this ground of deportation did not arise until 1952.

B. As noted earlier, Congress intended suspension of deportation of aliens within the scope of §1254(a)(1) to cease on December 31, 1957. Yet if both paragraphs (1) and (5) of §1254(a) apply to appellee, this avowed Congressional intention fails because appellee would be eligible for suspension after December 31, 1957, under paragraph (5). Moreover, the relief under paragraph (5) would not be available to appellee until ten years after the commission of his 1954 offense. Thus a very unusual hiatus occurs. For what reason would Congress desire an alien to be eligible for suspension for five years, not eligible for a longer period, and then eligible again? If this be what Congress intended, we can be sure that more explicit language to that effect would have been used.

C. It is also interesting to contrast the residence and moral character requirements of paragraph (1) and (5) of §1254(a) in the light of the "overlap" provisions of §1251(a)(5) and (17). In paragraph (5) of §1254(a), good moral character during a period of ten years residence within the United States following the commission of the act rendering one deportable is required. In paragraph (1), good moral character for a period of seven years residence within the United States prior to

the filing of application for suspension is all that is required. In paragraph (1) is Congress saying that good character may exist despite the commission of an act of deportation during the requisite seven years? Why this difference in language between paragraphs (1) and (5)?

It might be because the grounds of deportation in paragraph (5) are considered so serious that ten years good character after the ground arises is necessary before one is sufficiently "purged of his offense, but such purging is not required for minor offenses. Under this rationale, it would seem that the specific placement of §1251(a)(5) offenses in this category would mean necessarily that the easier provisions of relief in paragraph (1) were not intended to be available for such offenses.

On the other hand, there really may exist no disparity between the wording, when viewed closely. The only grounds of deportation arising after entry into the United States which are suspendable under paragraph (1) (other than the overlap provisions) are those listed in §1251 (a)(9) and (10). A brief reading of these sections in the Appendix will disclose readily that they could involve no lack of good moral character. Thus, if the overlap provisions are considered within paragraph (1), there arises the absurdity that offenses Congress considered heinous enough to place in the most undesirable category, where a "purging" is required, do not even constitute a lack of good character in paragraph (1). If the overlap provisions are said to be controlled exclusively by paragraph (5), however, the incongruity disappears.

In this respect, it should be noted that paragraphs (2) and (4) of §1254(a) specifically apply to grounds of deportation arising at or prior to entry; paragraphs

(3) and (5) specifically apply to grounds of deportation arising subsequent to entry. Paragraphs (2) and (4) require good moral character for a period of time "immediately preceding" the alien's application for suspension, whereas (3) and (5) require residence and good moral character to follow the commission of the act constituting the ground for deportation. Thus when paragraph (1) uses the language that is used in (2) and (4), *i. e.*, that seven years residence must be "immediately preceding the date of such application," it is patently clear that Congress considers paragraph (1) offenses to be those which arise at or prior to entry, as in paragraphs (2) and (4), and not subsequent to entry as in those in paragraphs (3) and (5). Since the overlap grounds for deportation arise subsequent to entry, it must have been Congressional intention to exclude such grounds from paragraph (1) relief.

D. Title 8, United States Code §1254(e), authorizes the relief of voluntary departure in lieu of deportation. The section is somewhat unclear at first reading, but has been administratively construed (*In the Matter of V.*, 6 Immigration and Nationality Decisions 723 1955)), and we believe properly so, as follows: Aliens within the provisions of paragraphs (4)-(7), 11, 12, (14)-(17), or (18) of Section 1251(a) of Title 8 are excluded from relief of voluntary departure unless such aliens satisfy the ten year physical presence and moral character requirements of 8 U. S. C. §1254(a)(4) or (5). Thus, once again Congress demonstrates that it regards the above-enumerated paragraphs of §1251(a) as being more heinous than others and that it has carefully restricted the relief granted aliens within the provisions of such paragraphs.

It is clear that Mr. Sevitt would not be eligible for the relief of voluntary departure, a lesser relief than suspension of deportation, where the alien is allowed to remain in this country, since he cannot satisfy the residence and moral character requirements of §1254(a)(5). However, if he is considered to be eligible for the greater relief of suspension of deportation under §1254(a)(1), the careful statutory restrictions upon relief to aliens in his category breaks down. Once again it seems crystal clear that an absurd result would occur if appellee's application for suspension of deportation can be considered under paragraph (1) of §1254(a). Only if paragraph (5) thereof is held to control exclusively can intelligent, uniform and consistent exercise of Congressional intent take place.

### Conclusion.

8 United States Code §1254(a)(5) alone should be held to govern the application of appellee for suspension of deportation. Such a holding would be in accordance with (1) the normal rule of construction concerning specific and general provisions, (2) the clear Congressional intent to severely limit relief to aliens deportable under §1251(a)(5), and (3) with a decision of the Court of Appeals for the Fifth Circuit precisely in point.

Respectfully submitted,

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The first of these is the fact that the  
 system is not a simple one, and that  
 the results are not always the same.

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## APPENDIX.

8 United States Code §1254 provides as follows:

*“§1254. Suspension of deportation—Adjustment of status for permanent residence; contents*

“(a) As hereinafter prescribed in this section, the Attorney General may, in his discretion, suspend deportation and adjust the status to that of an alien lawfully admitted for permanent residence, in the case of an alien who—

“(1) applies to the Attorney General within five years after the effective date of this chapter for suspension of deportation; last entered the United States more than two years prior to June 27, 1952; is deportable under any law of the United States and is not a member of a class of aliens whose deportation could not have been suspended by reason of section 19(d) of the Immigration Act of 1917, as amended; and has been physically present in the United States for a continuous period of not less than seven years immediately preceding the date of such application, and proves that during all of such period he was and is a person of good moral character; and is a person whose deportation would, in the opinion of the Attorney General, result in exceptional and extremely unusual hardship to the alien or to his spouse, parent or child, who is a citizen or an alien lawfully admitted for permanent residence; or

“(2) last entered the United States within two years prior to or at any time after June 27, 1952; is deportable under any law of the United States solely for an act committed or status existing prior to or at the time of such entry into the United States and is not within the provisions of paragraph (4) of this subsection; was

possessed of all of the requisite documents at the time of such entry into the United States; has been physically present in the United States for a continuous period of not less than five years immediately preceding his application under this paragraph, and proves that during all of such period he has been and is a person of good moral character; has not been served with a final order of deportation issued pursuant to this chapter in deportation proceedings up to the time of applying to the Attorney General for suspension of deportation; and is a person whose deportation would, in the opinion of the Attorney General, result in exceptional and extremely unusual hardship to the alien or to his spouse, parent, or child, who is a citizen or an alien lawfully admitted for permanent residence; or

“(3) last entered the United States within two years prior to, or at any time after June 27, 1952; is deportable under any law of the United States for an act committed or status acquired subsequent to such entry into the United States and is not within the provisions of paragraph (4) or (5) of this subsection; was possessed of all of the requisite documents at the time of such entry into the United States; has been physically present in the United States for a continuous period of not less than five years immediately following the commission of an act, or the assumption of a status, constituting a ground for deportation, and proves that during all of such period he has been and is a person of good moral character; has not been served with a final order of deportation issued pursuant to this chapter in deportation issued pursuant to this chapter in deportation proceedings up to the time of applying to the Attorney General for suspension of deportation; and is a person whose deportation would,

in the opinion of the Attorney General, result in exceptional and extremely unusual hardship to the alien or to his spouse, parent, or child, who is a citizen or an alien lawfully admitted for permanent residence; or

(4) last entered the United States within two years prior to, or at any time after June 27, 1952; is deportable under paragraph (1) of section 1251(a) of this title insofar as it relates to criminals, prostitutes or other immoral persons, subversives, violators of narcotic laws and similar classes or under paragraph (2) of section 1251(a) of this title, as a person who entered the United States without inspection or at a time or place other than as designated by the Attorney General, or without the proper documents and is not within the provisions of paragraph (5) of this subsection; has been physically present in the United States for a continuous period of not less than ten years after such entry and immediately preceding his application under this paragraph and proves that during all of such period he has been and is a person of good moral character; has not been served with a final order of deportation issued pursuant to this chapter in deportation proceedings up to the time of applying to the Attorney General for suspension of deportation; and is a person whose deportation would, in the opinion of the Attorney General, result in exceptional and extremely unusual hardship to the alien or to his spouse, parent, or child, who is a citizen or an alien lawfully admitted for permanent residence; or

(5) is deportable under paragraphs (4)-(7), (11), (12), (14)-(17), or (18) of section 1251(a) of this title for an act committed or status acquired subsequent to such entry into the United States or having last en-

tered the United States within two years prior to, or at any time after June 27, 1952. is deportable under paragraph (2) of section 1251(a) of this title as a person who has remained longer in the United States than the period for which he was admitted; has been physically present in the United States for a continuous period of not less than ten years immediately following the commission of an act, or the assumption of a status, constituting a ground for deportation, and proves that during all of such period he has been and is a person of good moral character; has not been served with a final order of deportation issued pursuant to this chapter in deportation proceedings up to the time of applying to the Attorney General for suspension of deportation; and is a person whose deportation would, in the opinion of the Attorney General, result in exceptional and extremely unusual hardship to the alien or to his spouse, parent, or child, who is a citizen or an alien lawfully admitted for permanent residence.

FULFILLMENT OF REQUIREMENTS OF PARAGRAPHS (1)-  
(3) OF SUBSECTION (A); REPORT TO CONGRESS

(b) Upon application by any alien who is found by the Attorney General to meet the requirements of paragraphs (1), (2), or (3) of subsection (a) of this section, the Attorney General may in his discretion suspend deportation of such alien. If the deportation of any alien is suspended under the provisions of this subsection, a complete and detailed statement of the facts and pertinent provisions of law in the case shall be reported to the Congress with the reasons for such suspension. Such reports shall be submitted on the first and fifteenth day of each calendar month in which Congress is in session.

If during the session of the Congress at which a case is reported, or, prior to the close of the session of the Congress next following the session at which a case is reported, either the Senate or the House of Representatives passes a resolution stating in substance that it does not favor the suspension of such deportation, the Attorney General shall thereupon deport such alien or authorize the alien's voluntary departure at his own expense under the order of deportation in the manner provided by law. If neither the Senate nor the House of Representatives shall, within the time above specified, pass such a resolution, the Attorney General shall cancel deportation proceedings. The provisions of this subsection relating to the granting of suspension of deportation shall not be applicable to any alien who is a native of any country contiguous to the United States or of any adjacent island, unless he establishes to the satisfaction of the Attorney General that he is ineligible to obtain a non-quota immigrant visa.

FULFILLMENT OF REQUIREMENTS OF PARAGRAPHS (4)  
OR (5) OF SUBSECTION (A); REPORT TO CONGRESS

(c) Upon application by any alien who is found by the Attorney General to meet the requirements of paragraph (4) or (5) of subsection (a) of this section, the Attorney General may in his discretion suspend deportation of such alien. If the deportation of any alien is suspended under the provisions of this subsection, a complete and detailed statement of the facts and pertinent provisions of law in the case shall be reported to the Congress with the reasons for such suspension. Such reports shall be submitted on the first and fifteenth day of each calendar month in which Congress is in session.

If during the session of the Congress at which a case is reported, or, prior to the close of the session of the Congress next following the session at which a case is reported, the Congress passes a concurrent resolution stating in substance that it favors the suspension of such deportation, the Attorney General shall cancel deportation proceedings. If within the time above specified the Congress does not pass such a concurrent resolution, or if either the Senate or House of Representatives passes a resolution stating in substance that it does not favor the suspension of the deportation of such alien, the Attorney General shall thereupon deport such alien in the manner provided by law.

#### RECORD OF CANCELLATION OF DEPORTATION

(d) Upon the cancellation of deportation in the case of any alien under this section, the Attorney General shall record the alien's lawful admission for permanent residence as of the date the cancellation of deportation of such alien is made, and the Secretary of State shall, if the alien was classifiable as a quota immigrant at the time of entry and was not charged to the appropriate quota, reduce by one the quota of the quota area to which the alien is chargeable under section 1152 of this title for the fiscal year then current at the time of cancellation or the next following year in which a quota is available. No quota shall be so reduced by more than 50 per centum in any fiscal year.

#### VOLUNTARY DEPARTURE

(e) The Attorney General may, in his discretion, permit any alien under deportation proceedings, other than an alien within the provisions of paragraphs (4)-

(7), (11), (12), (14)-(17), or (18) of section 1251(a) of this title (and also any alien within the purview of such paragraphs if he is also within the provisions of paragraph (4) or (5) of subsection (a) of this section), to depart voluntarily from the United States at his own expense in lieu of deportation if such alien shall establish to the satisfaction of the Attorney General that he is, and has been, a person of good moral character for at least five years immediately preceding his application for voluntary departure under this subsection. June 27, 1952, c. 477, Title II, ch. 5, §244, 66 Stat. 214.”

8 United States Code §1251(a)(5) provides as follows:

“§1251. *Deportable aliens—General Classes*

(a) Any alien in the United States (including an crewman) shall, upon the order of the Attorney General, be deported who—

\* \* \* \* \*

(5) has failed to comply with the provisions of section 1305 of this title unless he establishes to the satisfaction of the Attorney General that such failure was reasonably excusable or was not willful, or has been convicted under section 1306(c) of this title, or under section 36(c) of the Alien Registration Act, 1940, or has been convicted of violating or conspiracy to violate any provision of sections 611-621 of Title 22 or has been convicted under section 1546 of Title 18;”

8 United States Code §1305 provides as follows:

“§1305. *Change of address*

Every alien required to be registered under this subchapter, or who was required to be registered under the Alien Registration Act, 1940, as amended, who is within

the United States on the first day of January following the effective date of this chapter, or on the first day of January of each succeeding year shall, within thirty days following such dates, notify the Attorney General in writing of his current address and furnish such additional information as may by regulations be required by the Attorney General. Any such alien shall likewise notify the Attorney General in writing of each change of address and new address within ten days from the date of such change. Any such alien who is temporarily absent from the United States on the first day of January following the effective date of this chapter, or on the first day of January of any succeeding year shall furnish his current address and other information as required by this section within ten days after his return. Any such alien in the United States in a lawful temporary residence status shall in like manner also notify the Attorney General in writing of his address at the expiration of each three-month period during which he remains in the United States regardless of whether there has been any change of address. In the case of an alien for whom a parent or legal guardian is required to apply for registration, the notice required by this section shall be given by such parent or legal guardian. June 27, 1952, c. 477, Title II, ch. 7, §265, 66 Stat. 225.”

8 United States Code §1306 provides as follows:

“§1306. *Penalties—Willful failure to register*

(a) Any alien required to apply for registration and to be fingerprinted in the United States who willfully fails or refuses to make such application or to be fingerprinted, and any parent or legal guardian required to apply for the registration of any alien who willfully



fails or refuses to file application for the registration of such alien shall be guilty of a misdemeanor and shall, upon conviction thereof, be fined not to exceed \$1,000 or be imprisoned not more than six months, or both.

#### FAILURE TO NOTIFY CHANGE OF ADDRESS

(b) Any alien or any parent or legal guardian in the United States of any alien who fails to give written notice to the Attorney General, as required by section 1305 of this title, shall be guilty of a misdemeanor and shall, upon conviction thereof, be fined not to exceed \$200 or be imprisoned not more than thirty days, or both. Irrespective of whether an alien is convicted and punished as herein provided, any alien who fails to give written notice to the Attorney General, as required by section 1305 of this title, shall be taken into custody and deported in the manner provided by Part 5 of this subchapter, unless such alien establishes to the satisfaction of the Attorney General that such failure was reasonably excusable or was not willful.

#### FRAUDULENT STATEMENTS

(c) Any alien or any parent or legal guardian of any alien, who files an application for registration containing statements known by him to be false, or who procures or attempts to procure registration of himself or another person through fraud, shall be guilty of a misdemeanor and shall, upon conviction thereof, be fined not to exceed \$1,000, or be imprisoned not more than six months, or both; and any alien so convicted shall, upon the warrant of the Attorney General, be taken into custody and be deported in the manner provided in Part 5 of this subchapter.

## COUNTERFEITING

(d) Any person who with unlawful intent photographs, prints, or in any other manner makes, or executes, any engraving, photograph, print, or impression in the likeness of any certificate of alien registration or an alien registration receipt card or any colorable imitation thereof, except when and as authorized under such rules and regulations as may be prescribed by the Attorney General, shall upon conviction be fined not to exceed \$5,000 or be imprisoned not more than five years, or both. June 27, 1952, c. 477, Title II, ch. 7, §266, 66 Stat. 225."

8 United States Code §155 provided as follows:

"§155. *Deportation of undesirable aliens generally*

(a) At any time within five years after entry, any alien who at the time of entry was a member of one or more of the classes excluded by law; any alien who shall have entered or who shall be found in the United States in violation of this chapter, or in violation of any other law of the United States; any alien who at any time after entry shall be found advocating or teaching the unlawful destruction of property, or advocating or teaching anarchy, or the overthrow by force or violence of the Government of the United States or of all forms of law or the assassination of public officials; any alien who within five years after entry becomes a public charge from causes not affirmatively shown to have arisen subsequent to landing; except as hereinafter provided, any alien who, after May 1, 1917, is sentenced to imprisonment for a term of one year or more because of conviction in this country of a crime involving moral turpitude, committed within five years after the entry of the alien

to the United States, or who is sentenced more than once to such a term of imprisonment because of conviction in this country of any crime involving mortal turpitude, committed at any time after entry; any alien who shall be found an inmate of or connected with the management of a house of prostitution or practicing prostitution after such alien shall have entered the United States, or who shall receive, share in, or derive benefit from any part of the earnings of any prostitute; any alien who manages or is employed by, in, or in connection with any house of prostitution or music or dance hall or other place of amusement or resort habitually frequented by prostitutes, or where prostitutes gather, or who in any way assists any prostitute or protects or promises to protect from arrest any prostitute; any alien who shall import or attempt to import any person for the purpose of prostitution or for any other immoral purpose; any alien who, after being excluded and deported or arrested and deported as a prostitute, or as a procurer, or as having been connected with the business of prostitution or importation for prostitution or other immoral purposes in any of the ways hereinbefore specified, shall return to and enter the United States; any alien convicted and imprisoned for a violation of any of the provisions of section 138 of this title; any alien who was convicted, or who admits the commission, prior to entry, of a felony or other crime or misdemeanor involving moral turpitude; at any time within three years after entry, any alien who shall have entered the United States by water at any time or place other than as designated by immigration officials, or by land at any place other than one designated as a port of entry for aliens by the Commissioner of Immigration and Naturali-

zation, or at any time not designated by immigration officials, or who enters without inspection, shall, upon the warrant of the Attorney General, be taken into custody and deported. . . .

(b) Any alien of any of the classes specified in this subsection, in addition to aliens who are deportable under other provisions of law, shall, upon warrant of the Attorney General, be taken into custody and deported:

(1) Any alien who, at any time within five years after entry, shall have, knowingly and for gain, encouraged, induced, assisted, abetted, or aided any other alien to enter or to try to enter the United States in violation of law.

(2) Any alien who, at any time after entry, shall have on more than one occasion, knowingly and for gain, encouraged, induced, assisted, abetted, or aided any other alien or aliens to enter or to try to enter the United States in violation of law.

(3) Any alien who, at any time after entry, shall have been convicted of possessing or carrying in violation of any law any weapon which shoots or is designed to shoot automatically or semiautomatically more than one shot without manual reloading, by a single function of the trigger, or a weapon commonly called a sawed-off shotgun.

(4) Any alien who, at any time within five years after entry, shall have been convicted of violating the provisions of sections 9-13 of Title 18.

(5) Any alien who, at any time after entry, shall have been convicted more than once of violating the provisions of sections 9-13 of Title 18.

No alien who is deportable under the provisions of paragraph (3), (4), or (5) of this subsection shall be deported until the termination of his imprisonment or the entry of an order releasing him on probation or parole.

(c) In the case of any alien (other than one to whom subsection (d) is applicable) who is deportable under any law of the United States and who has proved good moral character for the preceding five years, the Attorney General may (1) permit such alien to depart the United States to any country of his choice at his own expense, in lieu of deportation, or (2) suspend deportation of such alien if not racially inadmissible or ineligible to naturalization in the United States if he finds that such deportation would result in serious economic detriment to a citizen or legally resident alien who is the spouse, parent, or minor child of such deportable alien. . . .

(d) The provisions of subsection (c) shall not be applicable in the case of any alien who is deportable under (1) section 137 of this title; (2) section 175 of Title 21; (3) section 156a of this title; (4) any of the provisions of so much of subsection (a) of this section as relates to criminals, prostitutes, procurers, or other immoral persons, the mentally and physically deficient, anarchists, and similar classes; or (5) subsection (b) of this section. Feb. 5, 1917, c. 29, §19, 39 Stat. 889; Ex. Ord. No. 6166, §14, June 10, 1933; Reorg. Plan No. V, eff. June 14, 1940, 5 Fed. Reg. 2423, 54 Stat. 1238; June 28, 1940, c. 439, Title II, §20, 54 Stat. 671."

8 United States Code §456 provided as follows:

“§456. *Notice of change of address*

“Any alien required to be registered under this chapter who is resident of the United States shall notify the Commissioner in writing of each change of residence and new address within five days from the date of such change. Any other alien required to be registered under this chapter shall notify the Commissioner in writing of his address at the expiration of each three months' period of residence in the United States. In the case of an alien for whom a parent or legal guardian is required to apply for registration, the notices required by this section shall be given by such parent or legal guardian. June 28, 1940, c. 439, Title III, §35, 54 Stat. 675.”

8 United States Code §457 provided as follows:

“§457. *Penalties*

(a) Any alien required to apply for registration and to be fingerprinted who willfully fails or refuses to make such application or to be fingerprinted, and any parent or legal guardian required to apply for the registration of any alien who willfully fails or refuses to file application for the registration of such alien shall, upon conviction thereof be fined not to exceed \$1,000 or be imprisoned not more than six months, or both.

(b) Any alien, or any parent or legal guardian of any alien, who fails to give written notice to the Commissioner of change of address as required by section 456 of this title shall, upon conviction thereof, be fined not to exceed \$100, or be imprisoned not more than thirty days, or both.

(c) Any alien or any parent or legal guardian of any alien, who files an application for registration containing statements known by him to be false, or who procures or attempts to procure registration of himself or another person through fraud, shall, upon conviction thereof, be fined not to exceed \$1,000; or be imprisoned not more than six months, or both; and any alien so convicted within five years after entry into the United States shall, upon the warrant of the Attorney General, be taken into custody and be deported in the manner provided in sections 155 and 156 of this title. June 28, 1940, c. 439, Title III, §36, 54 Stat. 675.”

8 United States Code §§1251(a)(5), (9) and (10) provide:

“§1251. *Deportable aliens—General classes*

“(a) Any alien in the United States (including an alien crewman) shall, upon the order of the Attorney General, be deported who—

\* \* \* \* \*

“(5) has failed to comply with the provisions of section 1305 of this title unless he establishes to the satisfaction of the Attorney General that such failure was reasonably excusable or was not willful, or has been convicted under section 1306(c) of this title, or under section 36(c) of the Alien Registration Act, 1940, or has been convicted of violating or conspiracy to violate any provision of sections 611-621 of Title 22 or has been convicted under section 1546 of Title 18;

\* \* \* \* \*

“(9) was admitted as a nonimmigrant and failed to maintain the nonimmigrant status in which he was ad-

mitted or to which it was changed pursuant to section 1258 of this title, or to comply with the conditions of any such status;

“(10) entered the United States from foreign contiguous territory or adjacent islands, having arrived there on a vessel or aircraft of a nonsignatory transportation company under section 1228(a) of this title and was without the required period of stay in such foreign contiguous territory or adjacent islands following such arrival (other than an alien who is a native-born citizen of any of the countries enumerated in section 1101(a)(27)(C) of this title and an alien described in section 1101(a)(27)(B) of this title);”



No. 15,644

IN THE  
United States Court of Appeals  
For the Ninth Circuit

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MARION S. FELTER, on behalf of himself and  
others similarly situated,

*Appellant,*

VS.

SOUTHERN PACIFIC COMPANY, a corporation;  
BROTHERHOOD OF RAILROAD TRAINMEN, a  
voluntary association; J. J. CORCORAN, as  
General Chairman, General Committee,  
Brotherhood of Railroad Trainmen; J. E.  
TEAGUE, as Secretary, General Committee,  
Brotherhood of Railroad Trainmen,

*Appellees.*

APPELLANT'S REPLY BRIEF.

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No. 15,644

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BROTHERHOOD OF RAILROAD TRAINMEN, a  
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Brotherhood of Railroad Trainmen,

*Appellees.*

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**APPELLANT'S REPLY BRIEF.**

---

**THE ULTIMATE ISSUE IS WHETHER THERE IS ANY AUTHORITY FOR THE CONTINUED DEDUCTION OF APPELLANT'S WAGES.**

The appellees state that the *sole* issue is whether the Dues Deduction Agreement places an unreasonable burden upon the exercise of an employee's right to change unions. The applicable law and the facts of this case do not support this assertion, which misdescribes the issue here.

The true issues that are involved are: --

(1) Section 2, Eleventh (c) prohibits agreements providing for deduction and payment of dues to a labor organization other than that in which an employee holds membership. It is undisputed that appellant *has* withdrawn his membership in the Brotherhood of Railroad Trainmen (hereinafter called BRT). Therefore, the legality of appellees' conduct in continuing to deduct and receive a portion of appellant's wages must be determined.

(2) Section 2, Eleventh (b) of the Railway Labor Act provides that an employee may revoke his wage assignment authorization a year after its execution. It is undisputed that appellant did submit a written revocation more than a year subsequent to signing his authorization. Hence, the legality of the continued deduction and receipt of appellant's wages must be determined.

With respect to the issue designated as (1) above, the answer of the BRT admits that appellant, on and after March 1, 1957,<sup>1</sup> was no longer a member of that labor organization (R. 7, 36). After having so admitted, the BRT places its refusal to honor appellant's revocation *solely* on the basis that the revocation "was not handled through the designated secretary and treasurer" of the BRT (R. 36). There thus can be no question that the BRT in this case is in-

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<sup>1</sup>The reference in the record at page 7 thereof to March 1, 1956, is obviously a typographical error, and should read March 1, 1957.

sisting upon, as a matter of law, the right to receive dues and other payments from an employee whom it admits is not a member of the BRT. This insistence and the actual receipt of such monies is a direct violation of Section 2, Eleventh (c) of the Act.

In this state of facts it matters not that appellee Southern Pacific Company may not have had actual proof of appellant's withdrawal from the BRT at the time it deducted dues from his wages and paid them over to the BRT. Both appellees rely upon an interpretation of the Dues Deduction Agreement which they maintain permits their conduct despite the admitted fact by the BRT that appellant was no longer its member. It is for this reason, among others, that appellant asserts that the Dues Deduction Agreement is invalid under the Act. The Act specifically provides that no such agreement may provide for deduction of dues and the like "*payable* to an organization other than that in which (an employee) holds membership." Yet appellees have so applied their Dues Deduction Agreement, contrary to the express provisions of the Act. It is, therefore, an unlawful agreement and neither appellee may escape this result by the argument that the Company had no proof that appellant was not a member of the BRT.

Manifestly, Congress did not intend that an employer could continue to deduct dues from an employee's wages and that a labor organization could continue to receive those dues for so long as the labor organization, with full knowledge of the fact, failed to advise the employer that the employee was not a

member of that union. And any agreement between the employer and the union which permits such a result, as it did here, is plainly in contravention of the Act.

Nor is this case controlled by *Pennsylvania R. R. Co. v. Rychlik*, 352 U.S. 480, cited by appellees, and that case is not in point to any issues in this case. The *Rychlik* case, *supra*, concerned the legality of a discharge under a union shop agreement. The Court merely held that in the exercise of the right to change unions, the union selected must be a labor organization which is "national in scope" in order to qualify under the Act; the term "national in scope" was interpreted to include only those unions qualified to elect representatives to the National Railroad Adjustment Board.

Whether or not appellant and others similarly situated had desired to change unions has no bearing on their rights under the Act as individual employees to revoke their dues deduction authorizations. These rights are as fully applicable to employees who choose to remain members of the union as they are to those who may decide to make a change. Such union members may pay dues directly to the union or decide to authorize deduction of dues from wages. The Act gives that choice only to the individual employee, and whichever choice is made only he may change it, and he may do it in the manner prescribed by the Act without interference from the union or the carrier. The holding in the *Rychlik* case, *supra*, is thus entirely beside the issue in the instant matter.



The critical issue here is whether the appellant, in revoking his dues deduction authorization, is entitled to the protection afforded by the provisions of the Act; and, if so, whether any legal justification may be found for the refusal of the appellees to give effect to that revocation.

In their briefs the appellees purport to find this justification in two provisions of the Dues Deduction Agreement:

(1) That revocations must be transmitted to the Company only through the BRT.

(2) That revocations must be on cards reproduced and furnished by the BRT.

Neither of these purposed "requirements" provides any semblance of justification for not terminating the wage deductions in accordance with appellant's revocation, and as required by Section 2, Eleventh (b) of the Act.

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**THE REFUSAL TO HONOR APPELLANT'S REVOCATION CANNOT BE JUSTIFIED ON THE GROUNDS THAT THE DUES DEDUCTION AGREEMENT REQUIRES REVOCATIONS TO BE SUBMITTED TO THE COMPANY THROUGH THE BRT.**

The Company, in its brief, devotes considerable space to arguing the desirability from its standpoint of having the BRT take the responsibility for processing all revocations (Company's Brief, pp. 7-8). The short answer to this contention might well be that the Company cannot so abdicate its responsibility as to deprive individual employees of their rights under the Act.

But more importantly, the record herein precludes any reliance on any such requirement. The fact is that the BRT had in its possession not one, but two revocation cards executed by the appellant. One of these cards was submitted directly to the BRT (R. 23-24, 67). The other card, sent by the appellant to the Company, was forwarded by the Company to the BRT for inclusion on the list "of employees from whose wages no further deductions (were) to be made" (R. 28-29, 67).

It is, therefore, apparent that this Dues Deduction Agreement provision, even if valid, provides no justification for the failure to give effect to appellant's revocation.

The BRT in its brief argues that it is not a burden for "a member to ask his union" for the revocation card. The very point involved is that appellant was *not* a member of the BRT and it was not "his union." The fact of this severance of membership relations goes to the heart of the realities of industrial relations life involved in this case. Appellant was a non member of the union and it became the interest of the BRT to place obstacles in his path, and the requirement that appellant submit himself to the grace of the BRT to get a release of his own money is *per se* coercive under the circumstances. Moreover, it is not true that the BRT "immediately" gave him that release "without comment" (BRT Brief, p. 11). The fact is that although it had in its possession appellant's revocation card in proper form, the BRT refused to send it to the Company, and instead appel-

lant was advised he would have to wait at least another month to be released of his wage assignment and then only if he made out and submitted to the BRT another identical card, differing only in that it was printed by the BRT. While appellant was thus forced to cool his heels at the whim of the BRT, he was told that the BRT "hoped" that he would "reconsider" (R. 25).

This was, indeed, the kind of "interference" which, if present, the BRT concedes would give grounds for maintaining appellant's rights under the law had been obstructed (BRT Brief, p. 12). Not many employees under such conditions would persevere in this battle of wits with a powerful union, and under normal conditions the BRT would succeed in such tactics. It is to prevent such practices against any employee who seeks to assert his individual rights under the law, that appellant has brought this action.

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**THE REFUSAL TO HONOR APPELLANT'S REVOCATION CANNOT BE JUSTIFIED ON THE GROUNDS THAT REVOCATIONS CAN BE MADE ONLY ON CARDS "REPRODUCED AND FURNISHED" BY THE BRT.**

Appellees in their briefs make continual reference to the necessity of establishing some "orderly procedure" as to the manner in which revocations must be made. This is said to be necessary in order to facilitate the requisite bookkeeping entries and changes in personnel records. It is noteworthy that Congress did not deem it necessary to prescribe any intricate revocation process. But even assuming

appellees' point is well taken, under the facts herein, no justification for the refusal to honor appellant's revocation may be found.

As found by the Court below, the revocation cards submitted were identical in form to those assertedly required by the Dues Deduction Agreement (R. 67). No contention is made that the precise information and data required to effect any changes in personnel records were not fully supplied. Nor is there any dispute as to the timeliness of the revocations.

The sole basis for the refusal is the fact that the revocation cards were not "reproduced and furnished" by the BRT. But the fact that the revocation cards were not printed at the expense of the BRT is totally unrelated to any administrative paper work required. Equally irrelevant to any necessary record keeping is whether the blank revocation card forms in the first instance are obtained from the BRT.

Thus, while appellees disclaim any intent to frustrate the employees' desire to discontinue the dues deduction, one may logically ask what then is the purpose of the requirement that only a revocation card granted at the grace of the BRT will be accepted?

Appellees contend for the "right" of the BRT to be "assured" that a revocation is "the result of a considered decision of the employee" (Company's Brief, pp. 8-9; BRT Brief, p. 11). The Act plainly does not contemplate that a union, with a real financial interest in the matter, shall sit in judgment as to whether the

revocation represents such a "considered decision." Congress did not intend that only such revocations are to be effective which, to the satisfaction of the union, are deemed executed with sufficient solemnity.

The BRT in its brief assumes unto itself the right to determine that the employee has not been the "victim of a raid" or has not been "high pressured" or "unduly influenced" (BRT Brief, p. 11). Presumably this means that if the BRT, a highly interested adverse party, decides that the employee has been "unduly influenced," it will refuse to act upon the revocation even though, admittedly, the employee involved is not a member of the BRT, and the revocation is in proper form. Thus, the control sought to be exercised here over the individual employee is real and it is serious. This intent to exercise a veto power over the individual employee is affirmed in strong terms by the appellees themselves in arguing to this Court that they be permitted to continue to enforce their Dues Deduction Agreement in this manner. Plainly, this is not what Congress had in mind when the provisions of the law here involved were adopted after it had been reiterated in the congressional debates that it was "*wholly and entirely* within the discretion of the employee" as to whether his union dues were to be deducted from his wages by an employer and paid over to a labor union (Appellant's Opening Brief, Appendix p. vi). By the Act, individual employees were carefully protected from this kind of union control over their free right to revoke dues deduction authorizations.

Equally unconvincing is appellees' argument that the requirement that revocation cards be secured from the BRT is necessary in order to preclude forgeries. Such reasoning, if followed, would enable unions to require that revocations be accompanied by verifying affidavits or to otherwise further stultify the intent of the law. No reason suggests itself why the Union rather than the Company is in a better position to detect forgery of an employee's signature. Congress thought it adequate that revocations be made in writing and did not intend that this right be nullified by the imposition of additional onerous or frustrating restrictions imposed by labor organizations or by private agreements between employers and unions, as in this case.

In view of the otherwise complete irrationality of requiring that revocation cards be "furnished" only by the BRT, the conclusion is irresistible that its purpose and effect can only be to enable the BRT to delay or frustrate revocations until such time as it is able to exert sufficient pressure on the employees, or confront them with so many obstacles that they will abandon their efforts.

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**APPELLANT IS NOT "BOUND" BY THE REVOCATION PROVISION OF THE DUES DEDUCTION AGREEMENT.**

The Company argues that the appellant is bound by the terms of whatever agreement the BRT, as collective bargaining representative, has entered into with the Company (Company's Brief, p. 11). In so

doing the Company ignores the very purpose which Congress evidenced in surrounding the check-off system with safeguards. The whole purpose in inserting the requirements of individual authorizations, and conferring the right of individual revocation, was to remove the check-off system from the exclusive control of carriers and labor organizations. In the words of Senator Hill, at the end of a year if an employee "does not like the way it works" he can put an end to his dues deduction (see Appellant's Opening Brief, Appendix, pp. vi, vii). That is all that appellant seeks here, and he has not been accorded that statutory right.

Obviously the BRT, as collective bargaining representative, could not enter into an agreement with the Company purporting to make wage assignment authorizations *irrevocable* and thereby bind the employees. It is equally clear that employees are not bound by provisions in agreements which serve no purpose other than to place obstacles in the path of freely exercising their right of revocation.

Appellees further argue that appellant by initially submitting his Wage Assignment Authorization "ratified and accepted" the terms of the Dues Deduction Agreement pertaining to revocation (Company's Brief, p. 11). This argument overlooks the express language of the Wage Assignment Authorization, which provides:

"This authorization may be revoked by the undersigned in writing, after the expiration of one (1) year, or after the termination date of the afore-

said deduction agreement, or upon the termination of the rules and working conditions agreement, whichever occurs sooner." (R. 78-79.)

Beyond the authorization which appellant signed there is nothing in this record to show that appellant ever saw the Dues Deduction Agreement or knew of its terms.

It is thus clear that no limitation was placed on the revocability of these authorizations or consented to by appellant, save those contained in the Railway Labor Act itself. No reference is made in the Wage Assignment Authorization which appellant signed to any requirement that revocation could be made only on cards which had been printed by the BRT, and which had been secured from that organization. Appellant, therefore, bound himself by his written consent only to what the Act specifies, and nothing more.

It is specious to argue that in executing these authorizations appellant thereby bound himself to revocation procedure assertedly required by the Dues Deduction Agreement. This is particularly true in view of the peculiar wording of that portion of the agreement relied upon by the appellees, Section 1(c). Section 1(c) is couched entirely in terms of determining responsibility as between the BRT and the Company (R. 75). On the other hand, that portion of the agreement dealing directly with revocation is Section 1(b) (R. 74-75). This section, as with the Wage Assignment Authorization, merely restates the express requirements of the Act with respect to the



elapsed period prior to revocation and that the revocation shall be in writing. The only additional requirement of this section of the Agreement is that revocations be in the form of Attachment "B" cards, and there is no dispute as to the fact that appellant's revocation was made in this form, even assuming the validity under the Act of such a requirement.

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### CONCLUSION.

Despite all of their protestations as to the "reasonableness" of their Dues Deduction Agreement, the fact remains that appellees have continued to deduct and receive portions of appellant's wages solely because of the fact that his revocation card was not first secured from the BRT, and despite the fact that appellant was not a member of the BRT, of which fact appellee BRT had direct knowledge.

A requirement such as this that an employee must run the gamut of obstacles placed in his way by the very organization from which he has severed connections, is inherently repugnant to accepted ideas of freedom of choice. If such a capricious rule as this is permitted under the law, then no end of clever devices can be hereafter constructed to hamstring an employee, once he has committed himself to having his dues deducted from his pay. Congress foresaw this problem when it unequivocally and unconditionally granted the full right of revocation to the individual employee. This right may not be tampered with under color of any excuse, either by carriers or

labor organizations who are subject to provisions of the Railway Labor Act.

We submit that the action of appellees in refusing to honor appellant's written dues deduction revocation is violative of the express language and purpose of the Railway Labor Act, and is in denial of appellant's rights thereunder.

Dated, San Francisco, California,  
April 14, 1958.

Respectfully submitted,  
CARROLL, DAVIS, BURDICK & McDONOUGH,  
By ROLAND C. DAVIS,  
*Attorneys for Appellant.*

No. 15644

In the

# United States Court of Appeals

*For the Ninth Circuit*

---

MARION S. FELTER, on behalf of himself  
and others similarly situated,

*Appellant,*

vs.

SOUTHERN PACIFIC COMPANY, a corporation;  
BROTHERHOOD OF RAILROAD TRAINMEN, a voluntary association;  
J. J. CORCORAN, as General Chairman, General Committee,  
Brotherhood of Railroad Trainmen;  
J. E. TEAGUE, as Secretary, General Committee,  
Brotherhood of Railroad Trainmen,

*Appellees.*

## Brief for Appellee Southern Pacific Company

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CORCORAN, as General Chairman, Gen-  
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road Trainmen; J. E. TEAGUE, as  
Secretary, General Committee, Brother-  
hood of Railroad Trainmen,

*Appellees.*

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## Brief for Appellee Southern Pacific Company

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### APPELLEE'S STATEMENT OF THE CASE

This is a suit for declaratory and injunctive relief brought pursuant to 28 U.S.C. 1332, 1337 and 2201, for the purpose of determining a question in actual controversy between appellant, Marion S. Felter and others similarly situated, and appellees, Southern Pacific Company (hereinafter referred to as the "Company") and Brotherhood of Railroad Trainmen (hereinafter referred to as "B.R.T."), to-wit, the ques-

tion of the validity under the Railway Labor Act (45 U.S.C. 152, Eleventh) of a written collective bargaining agreement which became effective August 1, 1955 (R. 74-80). This agreement, which is now and at all times material has been in effect between the Company and the B.R.T., provides in effect that the Company shall deduct sums for periodic dues, initiation fees, assessments and insurance (not including fines and penalties), payable to the B.R.T. by members thereof from "wages earned in any of the services or capacities covered in Section 3, First (h) of the Railway Labor Act defining the jurisdictional scope of the First Division, National Railroad Adjustment Board, upon the written and unrevoked authorization of a member in the form agreed upon by the parties hereto \* \* \*." This arrangement is commonly (and hereinafter) referred to as a "Dues Deduction Agreement." This Dues Deduction Agreement (R. 74-80) provides (in part):

"[1] (c). Both the authorization forms and the revocation of authorization forms shall be reproduced and furnished as necessary by the Organization without cost to the Company. *The Organization shall assume full responsibility for the procurement and execution of the forms by employes and for the delivery of such forms to the Company.*

2. *Deductions as provided for herein shall be made by the Company in accordance with certified deduction lists furnished to the Division Superintendent by the Treasurer of the Local Lodge of which the employe is a member. Such lists, together with assignment and revocation of assignment forms, shall be furnished to the Division Superintendent on or before the 5th day of each month in which the deduction or termination of deduction is to become effective as hereinafter provided. The original lists furnished shall show the employe's name, employe account number, and the amount to be deducted in the form approved by the Company.*



*Thereafter, two lists shall be furnished each month by the Treasurer of the Local Lodge to the Division Superintendent as follows:*

(a). A list showing any changes in the amounts to be deducted from the wages of employes with respect to whom deductions are already being made. Such list shall show both the amounts previously authorized to be deducted and the new amounts to be deducted; *also the names of employes from whose wages no further deductions are to be made which shall be accompanied by revocation of assignment forms signed by each employe so listed.* Where no changes are to be made the list shall so state.

(b). A list showing additional employes from whose wages the Company shall make deductions as herein provided, together with an assignment authorization form signed by each employe so listed. Where there are no such additional employes the list shall so state." (Emphasis supplied.)

The Company has scrupulously complied with the terms of the Dues Deduction Agreement.

Appellant and others similarly situated executed wage assignments in accordance with the Dues Deduction Agreement (R. 67). Thereafter, appellant and others submitted revocations of wage assignment to the Company and the B.R.T. (R. 67) which were neither reproduced nor furnished by the B.R.T. as required by the Dues Deduction Agreement (R. 24, 28, 74-75). Those revocations which were submitted to the Company were forwarded to the B.R.T. to be processed in accordance with the Dues Deduction Agreement (R. 28-30). Appellant was promptly notified by the B.R.T. that the revocation of assignment which he had submitted could not be accepted because it had not been reproduced and furnished by the B.R.T. as required by the Dues Deduction Agreement (R. 25). The B.R.T. then mailed to appel-

lant a form which would be accepted by the B.R.T. (R. 25). Appellant never returned the form furnished to him by the B.R.T. (R. 25-26).

On April 12, 1957, appellant filed complaint for declaratory and injunctive relief in the United States District Court (R. 1-10). Appellees B.R.T. and Southern Pacific Company filed answers (R. 35, 62). There being no substantial dispute as to the facts, the B.R.T. and the appellant moved for summary judgment or dismissal (R. 46-47, 59-61). On May 24, 1957, United States District Judge Edward P. Murphy (R. 65-70) held that "the dues deduction agreement as interpreted by the defendants is a reasonable compliance with the Railway Labor Act and not violative of plaintiff's rights under the Act", and dissolved the temporary restraining order and dismissed the action.

### ARGUMENT

- I. **As stated in the opinion of the District Court, the only question is whether the procedure established by the Dues Deduction Agreement places such an unreasonable burden on employees who wish to withdraw from the brotherhood that it operates as a violation of an employee's right to change unions under the Railway Labor Act.**

There is not, nor can there be, any dispute concerning interpretation of the Dues Deduction Agreement. The agreement is clear and explicit. It provides that revocations of wage assignments must be on forms "reproduced and furnished" by the B.R.T. and that the forms must be delivered to the Company through the B.R.T. (R. 75). The Court is concerned herein only with the question of whether these requirements are valid under Section 2, Eleventh of the Railway Labor Act (45 U.S.C. § 152, Eleventh).

Appellant, in his brief, points out that the Railway Labor Act provides that employees shall be free of "interference,

influence or coercion" in their choice of representatives (45 U.S.C. § 152, Third). Moreover, the Act also provides that nothing "shall prevent an employee from changing membership from one organization to another organization" (45 U.S.C. § 152, Eleventh (c)). However, the statement of appellant that the provisions of the Dues Deduction Agreement here under consideration constitute limitations not authorized by the Railway Labor Act and are "contrary to its entire design" is erroneous (Appellant's Brief, p. 9). There is absolutely nothing in the Railway Labor Act or in any other Act of Congress to indicate that the design of the Act or the intent of Congress was to insure that an employee would have absolute freedom to skip from one union to another. The purpose of the Railway Labor Act in insuring that certain employees may change unions has been clearly stated by the United States Supreme Court in *Pennsylvania R. Co. v. Rychlik*, 352 U.S. 480 (1957) as follows (p. 492) :

"It thus becomes clear that the only purpose of Section 2, Eleventh (c) was a very narrow one: to prevent compulsory dual unionism or the necessity of changing from one union to another when an employee temporarily changes crafts. The aim of the Section, which was drafted by the established unions themselves, quite evidently was not to benefit rising new unions by permitting them to recruit members among employees who are represented by another labor organization. Nor was it intended to provide employees with a general right to join unions other than the designated bargaining representative of their craft, except to meet the narrow problem of intercraft mobility. This is made particularly clear when the provision is taken in the context of American labor relations in general. The National Labor Relations Act contains no parallel to subsection (c), and employees under a union-shop

contract governed by that Act must join and maintain membership in the union designated as the bargaining representative or suffer discharge. Similarly, subsection (c) does not apply to *nonoperating* employees, where the problem of seasonal intercraft movement does not exist. Railroad employees such as clerks working under a union-shop contract have no right at all to join a union other than the bargaining representative. In other words, once a union has lawfully established itself for a period of time as the authorized bargaining representative of the employees under a union-shop contract, Congress has never deemed it to be a 'right' of employees to choose between membership in it and another competing union. If Congress intended to confer such a right, it would scarcely have denied the right to nonoperating employees of the railroads or industrial employees under the National Labor Relations Act. The purpose of Section 2, Eleventh (c) was simply to solve the problem of intercraft mobility under railroad union-shop contracts."

Thus, while the appellant in this case does have the privilege of changing unions, it cannot be contended that it was the intent of Congress to free the privilege of all restrictions no matter how reasonable they might be. Therefore, as correctly stated by the trial court (R. 69) :

"The only question is whether the procedure established by this agreement places such an unreasonable burden on employees who wish to withdraw from the Brotherhood that it operates as a violation of an employee's right under the Act to change unions."

**II. The provisions of the Dues Deduction Agreement comply with the Railway Labor Act and are not violative of appellant's rights under the Act.**

**A. The requirement that revocations be transmitted to the Company through the B.R.T. is reasonable and not violative of the Railway Labor Act.**

There are two separate requirements of the Dues Deduction Agreement. One is that the revocation must be on forms "reproduced and furnished" by the B.R.T. and the other is that the forms must be delivered to the Company through the B.R.T., together with certified deduction lists on or before the 5th day of the month in which the change in deductions is to become operative (R. 75). Clearly, appellee Company is vitally concerned with the latter requirement.

The Company receives no benefit whatever from the existence of a Dues Deduction Agreement. Such an agreement is solely for the benefit of the Organization and those employees who desire to avoid the inconvenience of making their own individual payments to the Organization of which they are members. Under such circumstances, it is only proper that the Union, the representative of the employee, should have the burden of insuring that revocations are not forgeries, take the responsibility for calculating the amounts to be deducted, be responsible for keeping accurate and up-to-date lists and do such other bookkeeping as does not necessarily need to be performed by the Company. In fact, such an arrangement clearly serves the purpose of avoiding disputes and controversies between the Union and the Company and is therefore in accord with the express purpose of the Railway Labor Act (45 U.S.C. § 152, First). Moreover, there is no requirement in the Railway Labor Act that the Company enter into a Dues Deduction Agreement, and it would undoubtedly be justified in refusing to make such an agreement, from which it derives absolutely no benefit, without the establishment of an orderly procedure. Unless

the Act contemplated the establishment of such an orderly procedure, it would seem unlikely that any Company would enter into a Dues Deduction Agreement and that portion of the statute allowing such agreements would become a nullity. Certainly Congress had no such intent.

It is clearly necessary that both the B.R.T. and the Company know when an employee revokes his existing authorization for the deduction of his dues, and the Union is obviously the logical party to receive and determine the validity of any revocation in the first instance. The requirement that revocations be transmitted to the Company through the B.R.T. in no way interferes with the right of the employee to make such revocations, and does not constitute a burden of any kind upon the employee. It is just as easy for the employee to send the revocation to the B.R.T. as it is to send it to the Company.

**B. The requirement that revocation forms be "reproduced and furnished" by the B.R.T. is reasonable and not violative of the Railway Labor Act.**

The Railway Labor Act (45 U.S.C. § 152, Eleventh (b)) says nothing as to the procedure to be followed in making deductions from wages except that authorizations and revocations thereof be in writing. However, it is obvious that some form of reasonable and orderly procedure must be established if confusion and misunderstandings are to be avoided or, at least, reduced to an absolute minimum. What the procedure shall be has been left to the parties when and if they "make agreements providing for the deduction".

The requirement that revocation forms be "reproduced and furnished" by the B.R.T. also serves another desirable objective. When the B.R.T. furnishes its own forms either in person or by mail to persons whom it knows to be members or former members, it may feel reasonably assured

when the correct form is returned that it is not a forgery and is the result of a considered decision of the employee. The B.R.T. has just as much right to be reasonably protected against spurious revocations as does the employee to make a revocation.

Certainly it is no more of a burden to ask the B.R.T. to provide appellant with the correct form than it would be for him to make such a request to some other union. Moreover, appellant voluntarily followed the agreement and obtained the correct form from the B.R.T. at the time he made his original authorization. What could be more logical than that he follow the same procedure when revoking the authorization?

Finally, it is difficult to see how requiring the appellant to request a correct form from the B.R.T. can constitute an unreasonable burden, or any burden at all, upon his right to change unions, since he obviously cannot change his union affiliation without informing the B.R.T. of his withdrawal.

**C. Appellant's failure to have his revocation accepted was due entirely to his own refusal to send in the correct form to the B.R.T.**

In his brief, appellant contends at length that if required to obtain the proper form from the B.R.T., he may be subjected to pressures not to revoke his wage assignment and above all not to change his union affiliation. However, there is absolutely nothing either in the record or in the Dues Deduction Agreement to give substance to these alleged fears. Appellee Southern Pacific Company concedes that if the B.R.T. refused or failed to furnish the correct and acceptable revocation forms upon request of the appellant, or if the B.R.T. refused to furnish such forms, unless and until the appellant submitted to efforts to persuade him not to change his union affiliation, the appellant would be sub-

jected to unreasonable burdens and would be entitled to effect a revocation of his wage assignment by other means.

However, such conduct, besides being an unreasonable burden upon the right of plaintiff to change unions, would also constitute a violation of the Dues Deduction Agreement itself. Clearly, the Dues Deduction Agreement contemplates that the B.R.T. shall have the acceptable forms in readiness and that the B.R.T. will furnish them promptly to an employee who wishes to revoke his wage assignment. Moreover, the record clearly demonstrates that the B.R.T. *did* have such forms available and *did* furnish the forms promptly to employees who requested them, including the appellant, without dilatory tactics of any kind. In fact, the record clearly shows that as soon as the B.R.T. became aware of the fact that appellant wished to revoke his wage assignment, the B.R.T. sent him the correct form to fill out even though appellant had never requested that the correct form be sent to him. Moreover, this form was mailed to him and no personal contact with the B.R.T. was requested or required (R. 25). Thus, despite all the appellant's protestations that the B.R.T. could refuse to furnish the forms or might refuse to furnish such forms except under circumstances whereby the appellant could be subjected to pressures not to change his union affiliation, the fact is that none of these contentions are supported by either the Dues Deduction Agreement itself, or by the actual facts. The only reason appellant failed to accomplish his objective of revoking his wage assignment, was his refusal to fill out and return the correct form, which was actually furnished to him by the B.R.T.



**D. Appellant should not be allowed to repudiate the contract which he has taken advantage of and which was made on his behalf by his collective bargaining representative.**

Appellant in this case is in the position of now attempting to disregard a contract which he has accepted and followed so long as he considered it convenient to do so. The B.R.T. in entering into the Dues Deduction Agreement acted as the chosen representative of the appellant. Agreements made by the collective bargaining representative are binding upon the employees represented by the B.R.T. *Atlantic Coast Line R.R. v. Pope*, 119 F. 2d 39 (4th Cir. 1941). Even if this were not true, appellant, by authorizing deductions from his wages pursuant to the agreement, ratified and accepted the terms thereof. Appellant knew the terms of the agreement because he obtained the correct form to make his original wage deduction authorization, nor has appellant ever contended that he didn't know that the agreement provided that the revocation forms were to be "reproduced and furnished" by the B.R.T. In other words, appellant knew the terms of the agreement; he knew he had to obtain the form from the B.R.T.; the B.R.T. voluntarily furnished him with the correct form, and the only reason appellant failed to have the Company cease making deductions from his wages in accordance with his original authorization was his apparently deliberate failure to follow the terms of the contract with which he was familiar and pursuant to which he had originally authorized the deductions.

### CONCLUSION

In summary, appellee Southern Pacific Company contends that a Dues Deduction Agreement may provide reasonable and orderly procedures governing its operation and the only right of appellant is to be free of unreasonable burdens

upon his privilege of changing unions. Moreover, both the Dues Deduction Agreement and the facts of this case show that the method of revocation is reasonable and serves the purpose of avoiding disputes in accordance with the express purpose of the Railway Labor Act and does not constitute an unreasonable burden upon appellant's privilege of changing unions. Therefore, it is respectfully submitted that the decision of the trial court is correct and should be affirmed.

Respectfully submitted,

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*Attorneys for Appellee,  
Southern Pacific Company.*

Dated: February 20, 1958.

No. 15,644

IN THE

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For the Ninth Circuit

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MARION S. FELTER, on behalf of himself and  
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General Chairman, General Committee,  
Brotherhood of Railroad Trainmen; J. E.  
TEAGUE, as Secretary, General Committee,  
Brotherhood of Railroad Trainmen,

*Appellees.*

APPELLANT'S OPENING BRIEF.

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**APPELLANT'S OPENING BRIEF.**

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**JURISDICTION.**

**District Court.**

The jurisdiction of the District Court in this case rests upon 28 U.S.C., Sections 1332, 1337, 2201. The plaintiff is a resident of the State of Oregon (R. 3, 35, 62). The defendant Southern Pacific Company (herein sometimes called Company) is a Delaware corporation doing business in California (R. 4-5, 35, 62). The defendant Brotherhood of Railroad Trainmen (herein sometimes called BRT) is a voluntary association do-

ing business in California (R. 4-5, 35, 62). The amount in controversy, exclusive of interest and costs, exceeds \$3,000.00 (R. 5, 35, 62). The case, therefore, is one involving diversity of citizenship for an amount in excess of the jurisdictional requirement, 28 U.S.C., Section 1291, and is also a suit arising under a law of the United States regulating commerce, the Railway Labor Act, 45 U.S.C.A., Section 151, et seq.

The existence of an actual controversy among the parties with respect to the validity under the Railway Labor Act of the Company's conduct in checking off dues in favor of the BRT from wages of employees who have withdrawn from said BRT and revoked their check-off authorizations, conferred jurisdiction on the District Court to declare the rights of the parties under the Federal Declaratory Judgment Act, 28 U.S.C., Section 2201.

Plaintiff has no administrative remedy through the National Railroad Adjustment Board, or otherwise, since there is no dispute concerning the interpretation of a collective bargaining agreement between the parties thereto. This is an action involving alleged infringement by the defendant carrier and the defendant labor organization of rights guaranteed to plaintiff by the Railway Labor Act. This action necessitates a determination of the validity of an agreement under the Railway Labor Act. Therefore, this action lies within the exclusive jurisdiction of the Federal District Court. *Brotherhood of Railroad Trainmen v. Howard*, 343 U. S. 768; *Tunstall v. Brotherhood of Locomotive Firemen and Enginemen*, 323 U. S. 210; *Steele*



*v. Louisville and Nashville R. R. Co.*, 323 U. S. 192; *Brotherhood of Locomotive Firemen and Enginemen v. Mitchell*, C.A. 5, 190 F. 2d 308; *Mount v. Grand International Brotherhood of Locomotive Engineers*, 6 Cir., 226 F. (2d) 604; *Primakow v. Railway Express Agency*, D.C. Wis., 57 F. Supp. 933.

In *Brotherhood of Railroad Trainmen v. Howard*, *supra*, a collective bargaining agreement was "construed and acted upon" by the railroad and the union as not permitting negro porters to continue to perform any of the duties of a brakeman (343 U. S. at 772). The Court held that the agreement was "to this extent illegal and unenforceable under the Railway Labor Act and that, therefore, the Court had both the jurisdiction and duty to enjoin the illegal acts."

#### **Court of Appeals.**

This is an appeal from a final decision of the United States District Court for the Northern District of California, Southern Division. This Court has jurisdiction of this appeal by virtue of 28 U.S.C., Section 1291.

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#### **STATEMENT OF THE CASE.**

Plaintiff-appellant and others similarly situated are employed by the defendant-appellee, Southern Pacific Company (R. 4). They were formerly members of the defendant-appellee Brotherhood of Railroad Trainmen (R. 6).

Effective August 1, 1955, the company and the BRT entered into a dues deduction agreement providing for

deduction of BRT dues and other fees by the Company upon written wage assignment authorizations by BRT members (R. 74-80).

On or before February 1, 1956, appellant and others similarly situated executed wage assignments authorizing the company to deduct sums for monthly dues and for other fees and pay them over to the BRT (R. 6, 35, 62). In compliance with Section 2, Eleventh, of the Railway Labor Act, 45 U.S.C.A. 152 (11), the assignments provided in part as follows (R. 78-79);

“This authorization may be revoked by the undersigned in writing, after the expiration of one year, or upon the termination date of the aforesaid deduction agreement, or upon the termination of the rules and working conditions agreement, whichever occurs sooner.”

More than a year after the expiration of these assignments, appellant and others resigned their membership in the BRT (R. 6, 35, 62). At the time of their resignations, these employees submitted written revocations of their wage assignments both to the Company and to the BRT (R. 6, 20-21, 23-24). The written revocations submitted by the appellant and others to the Company and to the BRT *were identical to the form of revocation attached to the dues deduction agreement* (R. 24, 79-80).

Notwithstanding the fact that the only requirement in the Railway Labor Act is that a revocation be “in writing”, and that the Act expressly provides that nothing shall prevent an employee from changing his

membership, the Company and the BRT refused to honor the written revocations of the appellant and others, and continued to deduct dues and pay them over to the BRT (R. 7-12, 29-33, 36). The refusal of the Company and the BRT was based on their interpretation of their dues deduction agreement as providing that a revocation could not be accomplished except upon prior application by the employee to the BRT for revocation forms which had been "reproduced and furnished" by the BRT (R. 25-33, 70-80). No contention was advanced that the revocations in any way failed to comply with the provisions of the Railway Labor Act (R. 24-33, 36-63).

This action was brought on behalf of plaintiff-appellant and others similarly situated for appropriate injunctive relief and a determination that the dues deduction agreement as interpreted and applied by the parties is invalid, and that the refusal of the Company and the BRT to accept appellant's written revocations of wage assignment is a violation of the rights of employees under the Railway Labor Act. Pending hearing on the issue, the Court below issued a temporary restraining order enjoining the Company from deducting any sums from wages due the appellant and others similarly situated and restraining the BRT from receiving such sums and professing to act as the collective bargaining agent for the appellant and others similarly situated (R. 15-16).

Substantially all of the allegations of the Complaint were admitted in the answer filed by the BRT (R. 35-37).

The facts not being in dispute, the appellant and the BRT moved for summary judgment (R. 46-47, 59-61).

The District Court was apparently of the opinion it was not enough that the employee send a written revocation as provided by the Railway Labor Act. It held that a change in dues deductions required "some sort of orderly procedure" and that while the requirement that a revocation card be secured from the BRT as a condition precedent to revocation was "a bit arbitrary", it was "no burden" and was "a reasonable compliance with the Railway Labor Act" (R. 69).

A final order dissolving the temporary restraining order and dismissing the action was accordingly entered on May 24, 1957 (R. 70). Timely notice of appeal was filed by appellant on June 10, 1957 (R. 70).

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### ARGUMENT.

**THE RAILWAY LABOR ACT PROVIDES WITHOUT LIMITATION THAT A WAGE ASSIGNMENT BY AN EMPLOYEE SHALL BE REVOCABLE IN WRITING AT ANY TIME AFTER THE EXPIRATION OF ONE YEAR.**

Section 2, Fourth, of the Railway Labor Act, as amended (45 U.S.C., 152, Fourth), insofar as it deals with a check-off of dues,<sup>1</sup> provides:

" \* \* \* it shall be unlawful for any carrier \* \* \* to deduct from the wages of employees any dues, fees, assessments, or other contributions payable to labor organizations."

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<sup>1</sup>The full provisions of Section 2, Fourth, and Eleventh, are set forth in the Appendix, *infra*, together with excerpts from the legislative history.

Section 2, Eleventh, of the Railway Labor Act (45 U.S.C., 152, Eleventh) excepts certain check-off agreements from the above proscription. In this regard the section reads:

“Notwithstanding any other provision of this chapter \* \* \* any carrier or carriers as defined in this chapter and a labor organization or labor organizations duly designated and authorized to represent employees in accordance with the requirements of this chapter shall be permitted

\* \* \* \* \*

“(b) to make agreements providing for the deduction by such carrier or carriers from the wages of its or their employees in a craft or class and payment to the labor organization representing the craft or class of such employees, of any periodic dues, initiation fees and assessments (not including fines and penalties) uniformly required as a condition of acquiring or retaining membership; Provided, That no such agreement shall be effective with respect to any individual employee until he shall have furnished the employer with a written assignment to the labor organization of such membership dues, initiation fees, and assessments, *which shall be revocable in writing after the expiration of one year or upon the termination date of the applicable collective agreement, whichever occurs sooner.*

“(c) \* \* \* no agreement made pursuant to subparagraph (b) shall provide for deduction from his wages for periodic dues, initiation fees, or assessments payable to any labor organization *other than that in which he holds membership* \* \* \* Provided, further That *nothing herein or in any such agreement or agreements shall prevent an*

*employee from changing membership from one organization to another organization admitting to membership employees of a craft or class in any of said services.'''\**

The case at bar presents a clear violation of an absolute right conferred upon employees governed by the Railway Labor Act. The Act guarantees the individual employees the right to discontinue dues deductions, the sole limitation being that the revocation be in writing.

The dues deduction agreement, as interpreted and applied by the BRT and the Company, seeks to impose additional limitations, that is, that the employee must first apply to the BRT for a revocation form which is "reproduced and furnished" by that organization. To secure such a form the employee obviously has to contact the local union officials before executing a dues revocation. He is thereby forced to go to the BRT officials and request them to furnish him a particular form for his use in discontinuing payment of dues to them. Such an agreement is designed to make it embarrassing to the employee to change his membership from the BRT and an employee bound by such a restriction cannot terminate dues deductions without first soliciting union grace and overcoming union dissuasion.

The purported requirement that as a condition precedent to revocation the employee first obtain a form "reproduced and furnished" by the BRT is a deterrent upon the employees' free choice of bargain-

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\*Emphasis supplied.

ing representatives. An employee who decides to discontinue his membership in the BRT is entitled to exercise this privilege without having to solicit help from the union or debate the wisdom of his decision with union officials.

The provision imposes limitations not authorized by the Railway Labor Act and is contrary to its entire design. In numerous provisions the Railway Labor Act enjoins all parties against "interference, influence or coercion" in choice of representatives. The employee is repeatedly assured of his right to exercise a free and untrammelled choice of bargaining representatives. One of the basic objectives of the Railway Labor Act is to provide for "the complete independence" of employees in the matter of self-organization. 45 U.S.C.A., Section 2. An employee who must rely on and request the grace of a union before he can leave it has lost some of his independence. It is the exact antithesis of the Railway Labor Act that an employee who desires a change in bargaining representative be dependent on some designated union to furnish him a form "reproduced" by it, and be forced to engage in a debate with the local officials before he can stop paying dues to that organization and choose another.

In representation elections, both under the Railway Labor Act and the Labor-Management Relations Act, the right of the employee to make his choice in secret is carefully preserved. An employee cannot secretly terminate his membership but it is his privilege and right to exercise this decision in the privacy of his

own thoughts independent of obstacles in his path. It is his privilege to exercise it without being forced to run the gauntlet of union embarrassment and dissuasion incident to requesting local union officials to furnish him a form "reproduced" by the union so that he can leave it.

Section 2, Fourth, of the Railway Labor Act prohibits dues deduction agreements and the sole authority for such agreements is derived from Section 2, Eleventh, of the Railway Labor Act. In Section 2, Eleventh, it is explicitly provided that there is no authority to deduct union dues after revocation in writing by the employee or after termination of membership in the assignee organization. Under these provisions, any written notice by the employee which contains a clear direction to revoke his wage assignment is in compliance with the Railway Labor Act.

The provisions of the Act lend no authority whatever for the proposition that the employee can be limited to a particular form of notice of revocation or that he can be restricted to procurement of a form from a particular union. The Act does not prescribe an involved procedure to which the employee must adhere in revoking his wage assignment. It requires only that the revocation be written, thereby excluding oral revocations. There is nothing in the Act which authorizes a carrier and a labor organization to enter into any elaborate recital of conditions as to how such revocations in writing shall be made.

If we assume, *arguendo*, that in the name of "orderly procedures" of bookkeeping, the carrier and a



labor organization may prescribe the form of writing to be used in revoking dues assignments, the record in this case provides no justification for the refusal to honor appellant's revocation. Appellant and other employees executed proper forms, made the deadline of "on or before April 5", and submitted executed revocation cards both to the Company and to the BRT (R. 7-20, 24, 28, 36, 79-80). Their one dereliction, in the view of the BRT, is that they did not use cards which were "reproduced and furnished" by that organization (R. 24, 30, 36).

So far as bookkeeping entries are involved, it was obviously irrelevant whether the revocation cards were "reproduced and furnished" by the BRT or were independently procured or prepared by the employees themselves. This is effectively demonstrated by the conduct of the Company in this case. The Company representative, having received appellant's revocation card along with the others, believed that they were in good order and should be honored. He promptly wrote the Secretary-Treasurer of the BRT local to that effect, saying (R. 28-29):

"The attached Wage Assignment Revocations are being forwarded to you \* \* \* as you will undoubtedly wish to show the same on the list to be furnished on or before the 5th day of April, 1957, as the names of employees from whose wages no further deductions are to be made."

The suggestion that Section 1(c) of the contract was devised because of orderly bookkeeping procedures is beside the mark. Both the carrier and the

BRT were furnished with exactly the same information on exactly the identical forms attached to the dues deduction agreement, which provided in paragraph 1 (b) in part as follows (R. 74):

“Revocation of the authorization shall be in the form agreed upon by the parties, copy of which is attached as Attachment ‘B’ and made a part hereof.”

Neither the Company nor the BRT made any objection based on bookkeeping procedures and neither objected as to the form of the revocation. Such objections would have been specious on this record. The BRT refusal was based solely on a tortured interpretation, to which the Company subsequently acceded, of Section 1 (c) of the dues deduction agreement which provides (R. 75):

“Both the authorization forms and the revocations of the authorization forms shall be reproduced and furnished as necessary by the organization without cost to the company. The organization shall assume full responsibility for the procurement and execution of the forms by employees and for the delivery of such forms to the company.”

The BRT seized on a portion of the language of Section 1 (c) with the claim that no revocation form was valid unless it had been “reproduced and furnished” by that organization. While it would appear that Section 1 (c) was inserted only for the purpose of relieving the Company of expenses and obligations in the administration of the check-off, the BRT insisted that this section of the agreement not only di-

vested the Company of any responsibility it might have, but also granted to the BRT the exclusive control of the revocation procedure as against the individual employee (R. 30). The Company then agreed with this contention (R. 7, 12, 63). The result is that the parties have construed the agreement not only as determining their responsibility *inter se*, but also as engrafting limitations on the statutory right of individual employees to submit written revocations of their wage assignments and to have such revocations acted upon with reasonable promptness.

Doubtless it was in the interest of the BRT to make it as difficult as possible for the individual employee to revoke his assignment of wages to that organization. But to say that such an agreement is not burdensome is to ignore realities. It is a deterrent on the freedom of the employee. The statutory right of revocation of dues assignments and the right to exercise a free choice of bargaining representative is as unequivocal and absolute as the right of free speech. The employee is not required to ask the union for permission to exercise his right of free speech and his freedom is not to be restricted by being compelled to make a request of the union before he can exercise his right to terminate an assignment of his wages or change membership.

If the Company and the union are entitled to engraft limitations on the employee's right of revocation of his wage assignment, such as the "form" of the revocation, then they can specify red paper, or 16 pound weight paper, or pica type, or whatever other condi-

tions ingenuity may devise in the name of "orderly procedure". The substantial interests of the union lie in devising a maze of restrictions to discourage individual employees from dues revocations.

To sustain the decision of the District Court is to amend the Railway Labor Act and engraft provisions thereon of an indefinite nature which Congress did not see fit to enact and which will inevitably be extended by whatever restrictions unions may subsequent devise. The judicial extension of such a power will not go unnoticed. In view of the stake, other means will be sought to tighten union check-off agreements so as to exercise a veto on the individual employee's right of revocation and free selection of another collective bargaining representative.

If the Courts are to pass in each case on the question of whether the particular restriction is "reasonable" or "unreasonable" and a "burden", an endless chain of litigation is in prospect. Congress did not intend the Railway Labor Act as an invitation to extensive litigation in the Courts over the merits or demerits of the revocation conditions in each check-off agreement executed by numerous separate unions with the various railroads of the United States. It was never the intent of the Railway Labor Act that recourse be had to the Courts as to whether each particular restriction on revocation in each union agreement is "reasonable" or a "burden". Congress sought only to protect the rights of the individual employee by providing a definite and simple procedure by which he might express his individual desire to discontinue dues deductions

and to change union membership without being bound for all time to pay dues to some union which negotiated a check-off agreement with the carrier.

We respectfully submit that the agreement, as interpreted and applied by the parties thereto, is void to the extent that it violates the provisions of the Railway Labor Act by unauthorized restrictions on the rights of individual employees.

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### CONCLUSION.

For the foregoing reasons, it is respectfully submitted that the order and judgment of the Court below should be reversed and the case remanded with directions to grant the relief requested in the complaint.

Dated, San Francisco, California,  
January 22, 1958.

CARROLL, DAVIS, BURDICK & McDONOUGH,  
*Attorneys for Appellant.*

(Appendix Follows.)



## **Appendix.**





## Appendix

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### THE STATUTE.

The pertinent provisions of the Railway Labor Act, as amended (Act of March 20, 1926, c. 347, 47 Stat. 577; Act of June 21, 1934, c. 691, 48 Stat. 1186; Act of Jan. 10, 1951, c. 1220, 64 Stat. 1238, 45 U.S.C. 151 et seq.) are as follows:

(These paragraphs are parts of 45 U.S.C. 152):

“Fourth. Employees shall have the right to organize and bargain collectively through representatives of their own choosing. The majority of any craft or class of employees shall have the right to determine who shall be the representative of the craft or class for the purposes of this chapter. No carrier, its officers or agents shall deny or in any way question the right of its employees to join, organize, or assist in organizing the labor organization of their choice, and it shall be unlawful for any carrier to interfere in any way with the organization of its employees, or to use the funds of the carrier in maintaining or assisting or contributing to any labor organization, labor representative, or other agency of collective bargaining, or in performing any work therefor, or to influence or coerce employees in an effort to induce them to join or remain or not to join or remain members of any labor organization, or to deduct from the wages of employees any dues, fees, assessments, or other contributions payable to labor organizations, or to collect or to assist in the collection of any such dues, fees, assessments, or other contributions: Provided, That

nothing in this chapter shall be construed to prohibit a carrier from permitting an employee, individually, or local representatives of employees from conferring with management during working hours without loss of time, or to prohibit a carrier from furnishing free transportation to its employees while engaged in the business of a labor organization.

“Eleventh. Notwithstanding any other provisions of this chapter, or of any other statute or law of the United States, or Territory thereof, or of any State, any carrier or carriers as defined in this chapter and a labor organization or labor organizations duly designated and authorized to represent employees in accordance with the requirements of this chapter shall be permitted—

“(a) to make agreements, requiring, as a condition of continued employment, that within sixty days following the beginning of such employment, or the effective date of such agreements, whichever is the later, all employees shall become members of the labor organization representing their craft or class: Provided, That no such agreement shall require such condition of employment with respect to employees to whom membership is not available upon the same terms and conditions as are generally applicable to any other member or with respect to employees to whom membership was denied or terminated for any reason other than the failure of the employee to tender the periodic dues, initiation fees, and assessments (not including fines and penalties) uniformly required as a condition acquiring or retaining membership.

“(b) to make agreements providing for the deduction by such carrier or carriers from the wages of its or their employees in a craft or class and payment to the labor organization representing the craft or class of such employees, of any periodic dues, initiation fees, and assessments (not including fines and penalties) uniformly required as a condition of acquiring or retaining membership: Provided, That no such agreement shall be effective with respect to any individual employee until he shall have furnished the employer with a written assignment to the labor organization of such membership dues, initiation fees, and assessments, which shall be revocable in writing after the expiration of one year or upon the termination date of the applicable collective agreement, whichever occurs sooner.

“(c) The requirement of membership in a labor organization in an agreement made pursuant to subparagraph (a) of this paragraph shall be satisfied, as to both a present or future employee in engine, train, yard, or hostling service, that is, an employee engaged in any of the services or capacities covered in the First Division of paragraph (h) of section 153 of this title, defining the jurisdictional scope of the First Division of the National Railroad Adjustment Board, if said employee shall hold or acquire membership in any one of the labor organizations, national in scope, organized in accordance with this chapter and admitting to membership employees of a craft or class in any of said services; and no agreement made pursuant to subparagraph (b) of this paragraph shall

provide for deductions from his wages for periodic dues, initiation fees, or assessments payable to any labor organization other than that in which he holds membership; Provided, however, That as to an employee in any of said services on a particular carrier at the effective date of any such agreement on a carrier, who is not a member of any one of the labor organizations, national in scope, organized in accordance with this chapter and admitting to membership employees of a craft or class in any of said services, such employee, as a condition of continuing his employment, may be required to become a member of the organization representing the craft in which he is employed on the effective date of the first agreement applicable to him; Provided, further, That nothing herein or in any such agreement or agreements shall prevent an employee from changing membership from one organization to another organization admitting to membership employees of a craft or class in any of said services.

“(d) Any provisions in paragraphs Fourth and Fifth of this section in conflict herewith are to the extent of such conflict amended. May 20, 1926, c. 347, § 2, 44 Stat. 577; June 21, 1934, c. 691, § 2, 48 Stat. 1186; June 25, 1948, c. 646, § 1, 62 Stat. 909; Jan. 10, 1951, c. 1220, 64 Stat. 1238.”

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#### LEGISLATIVE HISTORY.

As shown above, Section 2, Fourth, of the Railway Labor Act, as amended in 1934, prohibited all check-

ing off of dues to any labor organization. In 1951 Congress adopted Section 2, Eleventh, which expressly modifies Section 2, Fourth, to permit checking off of dues to the extent therein set forth. The legislative history of that section shows that Congress intended that the operation of the check-off system be subject to the control of the individual employees rather than to contracts between carriers and labor organizations.

The bills upon which hearings were held in Congress, preceding enactment of Section 2, Eleventh, were S. 3295, 81st Cong., 2nd Sess., and H.R. 7789, 81st Cong., 2nd Sess. These bills enabled carriers and labor organizations to enter into collective bargaining agreements providing for the check-off system. Neither bill, however, as originally introduced, required that the individual employee give his assent to the deductions from his wages.<sup>2</sup>

Although the Senate Bill was unanimously reported out of committee, Senator Taft and other members did not feel that the bill afforded adequate protection to the individual employees, such as is contained in the National Labor Relations Act.<sup>3</sup> Subsequent to the reporting of the bill and prior to debate on the matter, Senator Taft and Senator Hill devised certain amend-

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<sup>2</sup>S. 3295 as introduced is printed in Hearings Before a Subcommittee of the Committee on Labor and Public Welfare, U. S. Senate, on S. 3295, p. 1, 81st Cong., 2nd Sess. (1950). H.R. 7789 as introduced is printed in Hearings Before the Committee on Interstate and Foreign Commerce, House of Representatives, on H.R. 7789, p. 1, 81st Cong., 2nd Sess. (1950).

<sup>3</sup>Supplemental Views of Senators Taft, Smith and Donnell, S. Rep. No. 2262, 81st Cong., 2nd Sess., 1950. See also 96 Cong. Rec. 16267.

ments to the bill which made the wage deductions dependent upon the individual authorizations of the employees rather than upon the collective bargaining agreements between the carriers and the labor organizations.<sup>4</sup> Senator Hill, manager of the bill, explained the effect of the bill as amended to members of the Senate concerned about the rights of the individual employees.<sup>5</sup>

“The bill would also permit a carrier and a labor organization duly authorized to represent employees under the Act to enter into agreements providing for the check-off from wages of employees of periodic dues, initiation fees and assessments. But no such agreement is to be effective with respect to any individual employee unless first authorized in writing by him to the employer.

“Mr. Lucas. Is it not a fact that it is absolutely within the discretion of the employee as to whether he requests the check-off?

“Mr. Hill. It is wholly and entirely within the discretion of the employee, and unless the employee sits down and writes on *a piece of paper* an authorization to the employer to turn dues, fees and assessments over to the labor organization and signs his name to the authorization there is no check-off so far as the employee is concerned.” (Emphasis added.)

Also pertinent in this regard is the following exchange between Senator Wiley and Senator Hill:

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<sup>4</sup>96 Cong. Rec. 15735.

<sup>5</sup>96 Cong. Rec. 15736-15737.

“Mr. Wiley. I was interested in one phase of the question. I have been in contact with a number of laboring men. I talked with many of them during my campaign. I should like to know what the Senator’s statement was in relation to the check-off and whether that is compulsory. Some laboring men who have spoken to me, men who are good union members, have stated they do not like the system very well. The Senator said something to the effect that they must indicate in writing their choice or willingness or desire.

“Mr. Hill. \* \* \* In other words, before a single penny can be deducted from the salary of the individual employee for the normal dues or assessments, he must give a written assignment to the company, so that it can pay that money to the union. *Then he has a right, within a year, to revoke that assignment if he does not like the way it works, or if he wants to put an end to the deduction.*” (Emphasis added.)

Similarly when the bill reached the House its sponsors were careful to point out the protection afforded individual employees through the right of revocation.<sup>6</sup>

The foregoing legislative history demonstrates that Congress specifically rejected proposals which would have left the operation of the check-off system subject solely to the various provisions of collective bargaining agreements between the carriers and the unions, such as the “dues deduction agreement” here in question.

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<sup>6</sup>See Comments of Mr. Wolverton, 96 Cong. Rec. 17051.

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No. 15645

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**United States  
Court of Appeals  
For the Ninth Circuit**

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**HAROLD M. KOCH, BESSIE KOCH, WIL-  
LIAM L. KOCH, ROSE KOCH, REBECCA  
KOCH ABEL, MAURICE P. KOCH and  
DAISY KOCH,**

**Appellants,**

**vs.**

**UNITED STATES OF AMERICA,**

**Appellee.**

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**Transcript of Record**

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**Appeal from the United States District Court for the  
Northern District of California,  
Southern Division.**

**FILED**

**OCT 10 1957**

**PAUL P. GIBNEY, CLERK**



No. 15645

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

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Post Office Building,  
San Francisco, California,

For Appellee.

THE UNIVERSITY OF CHICAGO

PHYSICS DEPARTMENT

1952

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In the United States District Court for the Northern District of California, Southern Division

No. 34762—Civil

HAROLD M. KOCH, BESSIE KOCH, WILLIAM L. KOCH, ROSE KOCH, REBECCA KOCH ABEL, MAURICE P. KOCH and DAISY KOCH,

Plaintiffs,

vs.

UNITED STATES OF AMERICA,

Defendant.

EXCERPT FROM DOCKET ENTRIES

1955

July 5—Filed complaint with demand for jury trial and issued summons.

\* \* \*

Oct. 24—Filed answer by defendant.

\* \* \*

1956

July 23—Ordered for jury trial Sept. 17, 1956.

Sept. 13—Ordered case continued to Nov. 12, 1956, for trial.

Sept. 19—Ordered case continued to Nov. 13, 1956, for trial.

\* \* \*

Nov. 26—Jury trial. Jury impaneled, evidence and exhibits introduced and further trial continued to Nov. 27, 1956.

1956

- Nov. 27—Further jury trial. Evidence and exhibits introduced and further trial continued to Nov. 28, 1956, at 10 a.m.
- Nov. 28—Further jury trial. Evidence and exhibits introduced; motion of United States to amend Par. 2, of 11 & 13 counts of answer denied; motion of U.S.A. for directed verdict as to \$15,000.00 advanced by Maurice P. Koch granted; motion for directed verdict as to remainder of money advanced by H. Koch & Sons denied and further trial continued to Nov. 29, 1956.
- Nov. 29—Further jury trial. Arguments heard, jury retired and returned verdict for defendant. Motion of plaintiff for judgment notwithstanding verdict, continued to Nov. 30, 1956, at 10:30 a.m. Counsel for defendant to prepare findings, conclusions and form of judgment.
- Nov. 29—Filed verdict.
- Nov. 30—Arguments on motion for judgment notwithstanding verdict and motion to set aside special verdict. Both motions submitted.
- Dec. 3—Filed order denying motion of plaintiff for judgment notwithstanding verdict and to set aside verdict.
- Dec. 6—Lodged findings of fact and conclusions of law by defendant.
- Dec. 6—Lodged Judgment on special verdict by defendant.

1956

Dec. 28—Lodged findings of fact and conclusions of law by plaintiff.

1957

Jan. 23—Filed findings & conclusions (prepared by Court).

Jan. 23—Entered judgment on special verdict—filed Jan. 23, 1957, that plaintiff take nothing by their complaint and judgment awarded U.S.A. for costs.

Jan. 23—Mailed notices.

Jan. 25—Filed memorandum of costs by defendant (\$106.00).

Jan. 29—Costs taxed \$106.00.

Feb. 1—Filed notice and motion by plaintiff for new trial, Feb. 21, 1957.

\* \* \*

Feb. 21—Ordered after hearing motion for new trial submitted.

Mar. 5—Filed order denying motion for new trial.

\* \* \*

Apr. 18—Filed notice of appeal by plaintiff.

Apr. 18—Filed appeal bond in sum \$250.00.

Apr. 19—Mailed notices.

May 21—Filed order extending time to docket appeal to June 30, 1957.

June 18—Filed order extending time to docket appeal to July 17, 1957.

June 8—Filed appellants' designation of record on appeal.

[Title of District Court and Cause.]

### SPECIAL VERDICT

During the year 1947, was H. Koch and Sons regularly engaged in the business of financing motion picture ventures?

Answer: "No."

/s/ CHARLES L. PHIPPS,  
Foreman.

[Endorsed]: Filed November 29, 1956.

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[Title of District Court and Cause.]

### ORDER

The plaintiffs' motion for judgment notwithstanding the verdict and for setting aside the special verdict may be denied.

Dated: December 3, 1956.

/s/ O. D. HAMLIN,  
United States District Judge.

[Endorsed]: Filed December 3, 1956.

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[Title of District Court and Cause.]

### FINDINGS OF FACT AND CONCLUSIONS OF LAW

The above-entitled action came on regularly for trial on November 26, 1956; November 27, 1956; No-

vember 28, 1956; and November 29, 1956, before the Court and a jury duly impaneled and sworn, Honorable O. D. Hamlin, United States District Judge presiding. Max Fink, Esq., and Leon Schiller, Esq., appeared for plaintiffs and Lloyd H. Burke, Esq., United States Attorney, by Lynn J. Gillard, Esq., Assistant United States Attorney, appeared for defendant. Oral and documentary evidence was introduced and stipulations were made between respective counsel. The Court granted a directed verdict against the plaintiff Maurice P. Koch. Pursuant to stipulation, after instructions by the Court, a single interrogatory was submitted to the jury on November 29, 1956, and all other matters were left to the determination by the Court. The single interrogatory submitted to the jury and the special verdict thereon rendered by the jury is as follows:

“During the year 1947, was H. Koch & Sons regularly engaged in the business of financing motion picture ventures?

Answer: No.”

On the basis of the evidence and stipulations, the Court makes the following:

### FINDINGS OF FACT

1. The plaintiffs, Harold M. Koch, William L. Koch, Rebecca Koch Abel and Maurice P. Koch are brothers and sister. The said plaintiffs entered into a partnership pursuant to written agreement on December 31, 1941, and ever since said date have con-

tinued as partners under the firm name and style H. Koch & Sons.

2. The written articles of co-partnership of December 31, 1941, provided that the partnership would engage in the business of manufacturing luggage. Said articles of co-partnership were amended by written agreement dated October 23, 1944, pursuant to which the partners agreed to also engage in the business of financing motion picture productions. The said partnership agreement, as amended, has remained in full force and effect at all times herein mentioned.

3. The plaintiff, Bessie Koch, is the wife of the plaintiff Harold Koch; the plaintiff Rose Koch is the wife of William L. Koch; and the plaintiff Daisy Koch is the wife of the plaintiff Maurice P. Koch.

4. The above-entitled action was brought by plaintiffs to recover income taxes assessed and collected by defendant for the years 1945 and 1947, pursuant to the provisions of the Internal Revenue Code of 1939.

5. For the years 1945, 1946 and 1947, Maurice P. Koch, William L. Koch, Harold M. Koch and Rebecca Koch Abel were partners in the business of manufacturing and selling luggage, doing business under the firm name of H. Koch & Sons.

6. In 1946, H. Koch & Sons loaned \$75,000.00 to Beacon Pictures Corporation. As consideration for

the use of its money, H. Koch & Sons was to receive from the Beacon Pictures Corporation 6% interest per annum and a percentage of the profits of a film to be made, named Copacabana. The entire \$75,000.00 loan became worthless in 1947, and each partner's share of the loss was \$18,750.00.

7. The partnership of H. Koch & Sons timely filed a partnership income tax return for the year 1947, indicating a net income of \$19,223.19. Thereafter, an amended return was filed indicating a net loss of \$55,776.82 which resulted from a deduction of the \$75,000.00 loss.

8. Each of the plaintiffs timely filed individual income tax returns for the calendar years 1945 and 1947 with the United States Collector of Internal Revenue for the First District of California. Each of the plaintiffs filed with the same Collector original and amended claims for refund of taxes paid for the years 1945 and 1947 as follows:

	Original	1945 Amended	Original	1947 Amended
Harold M. Koch.....	\$ 3,623.90	\$ 3,623.90	\$223.00	\$223.00
Bessie Koch .....	3,673.08	3,673.08	318.00	318.00
William L. Koch.....	3,623.90	3,623.90	223.00	223.00
Rose Koch .....	3,673.08	3,673.08	318.00	318.00
Rebecca Koch Abel...	12,142.17	12,142.17	605.61	605.61
Maurice P. Koch.....	4,649.77	4,649.77	860.62	860.62
Daisy Koch .....	4,797.74	4,797.74	860.63	860.63

The Collector advised each of the plaintiffs that the claims for the year 1945 were denied, and that the claims for the year 1947 would not be allowed on the theory advanced to support the claims, but would be

allowed as a non-business bad debt and not otherwise.

9. The loss sustained by H. Koch & Sons and its respective partners in the year 1947 by reason of the said sums thus advanced resulted from a non-business bad debt.

10. Maurice P. Koch was not engaged in the business of financing motion picture ventures during the calendar year 1947.

11. In the complaint, the plaintiffs raised, among others, the following issues: (1) that the \$75,000.00 loss by the partnership of H. Koch & Sons and the alleged \$15,000.00 loss by Maurice P. Koch and Daisy Koch were incurred in the business of producing motion pictures or in a joint venture and (2) that the \$75,000.00 loss by the partnership of H. Koch & Sons and the alleged \$15,000.00 loss by Maurice P. Koch and Daisy Koch were incurred in a business regularly carried on other than the business of financing motion picture ventures. By stipulation of the parties prior to submission of the case to the jury the above issues were withdrawn.

12. The parties stipulated that the plaintiffs rights to recover the alleged overpayments of taxes would require the jury to answer "yes" to the following interrogatory submitted to them:

"During the year 1947, was H. Koch & Sons regularly engaged in the business of financing motion picture ventures?"



On the basis of the answer to the special interrogatory submitted to the jury, the stipulations made by the parties and the foregoing findings of fact, the Court makes the following:

### CONCLUSIONS OF LAW

1. The \$75,000.00 loss incurred by H. Koch & Sons in the year 1947 was not a loss incurred in the trade or business of H. Koch & Sons or incurred in any transaction entered into for profit, within the meaning of Section 23(e) of the Internal Revenue Code of 1939.

2. The \$15,000.00 loss alleged to have been individually suffered by Maurice P. Koch and Daisy Koch was not a loss incurred in a trade or business or incurred in any transaction entered into for profit, within the meaning of Section 23(e) of the Internal Revenue Code of 1939.

3. The \$75,000.00 loan to Beacon Pictures Corporation by H. Koch & Sons which became worthless in 1947 was a nonbusiness debt within the meaning of Section 23(k) of the Internal Revenue Code of 1939.

4. The \$15,000.00 loan made by Maurice P Koch and Daisy Koch, individually, which became worthless in the year 1947 was a nonbusiness debt within the meaning of Section 23(k) of the Internal Revenue Code of 1939.

5. The \$75,000.00 loss suffered by H. Koch & Sons in the year 1947 is not an allowable deduction

in arriving at the net operating loss pursuant to the provisions of Section 122 of the Internal Revenue Code of 1939.

6. The \$15,000.00 loss suffered by Maurice P. Koch and Daisy Koch in the year 1947 is not an allowable deduction in arriving at the net operating loss pursuant to the provisions of Section 122 of the Internal Revenue Code of 1939.

7. The income taxes assessed and collected from plaintiffs by defendant for the years 1947 and 1945 were validly assessed and collected pursuant to the provisions of the Internal Revenue Code of 1939.

8. The defendant the United States of America is entitled to judgment that plaintiffs recover nothing and that defendant recover its costs incurred.

Dated: January 23, 1957.

/s/ O. D. HAMLIN,

United States District Judge.

[Endorsed]: Filed January 23, 1957.

In the District Court of the United States for the  
Northern District of California, Southern Di-  
vision.

No. 34762

HAROLD M. KOCH, BESSIE KOCH, WILLIAM  
L. KOCH, ROSE KOCH, REBBECA KOCH  
ABEL, MAURICE P. KOCH and DAISY  
KOCH,

Plaintiffs,

vs.

UNITED STATES OF AMERICA,

Defendant.

### JUDGMENT ON SPECIAL VERDICT

The above-entitled action came on regularly for trial on November 26, 1956; November 27, 1956; November 28, 1956; and November 29, 1956, before the Court and jury empaneled and sworn, Honorable O. D. Hamlin, United States District Judge presiding. Max Fink, Esq., and Leon Schiller, Esq., appeared for plaintiffs, and Lloyd H. Burke, Esq., United States Attorney, by Lynn J. Gillard, Esq., Assistant United States Attorney, and Marvin D. Morgenstein, Esq., Assistant United States Attorney, appeared for defendant. Oral and documentary evidence was introduced and stipulations were made by respective counsel that the jury should be required to return a special verdict in the form of a finding on the issue of fact. Counsel for plaintiff and defendant thereupon stipulated that a special verdict be

returned in the form of an answer to the written interrogatory hereinafter set forth and that all other issues in the case would be determined by the Court.

After argument by respective counsel, and instructions by the Court having been given to the jury for consideration in answering the interrogatory, and the jury on the 29th day of November, 1956, having returned its special verdict which was as follows:

“During the year 1947, was H. Koch & Sons regularly engaged in the business of financing motion picture ventures?

Answer: No.

/s/ CHARLES L. PHIPPS,  
Foreman.”

And the Court having directed a verdict in favor of the defendant against Maurice P. Koch and Daisy Koch for the portion of the claims based upon the individual loan of \$15,000 by Maurice P. Koch; and having denied plaintiffs' motions for judgment notwithstanding the verdict and to set aside the special verdict; and the Court having made findings of fact and having found as a conclusion of law that by reason of the directed verdict and the special verdict and the findings of fact, plaintiffs are entitled to take nothing by their complaint and that judgment should be entered in favor of defendant.

It Is Hereby Ordered, Adjudged and Decreed that plaintiffs take nothing by their complaint, and

that judgment is awarded to defendant United States of America, together with its costs in this action amounting to the sum of \$106.00.

Dated: January 23, 1957.

/s/ O. D. HAMLIN,  
United States District Judge.

[Endorsed]: Filed and entered January 23, 1957.

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[Title of District Court and Cause.]

FINDINGS OF FACT AND CONCLUSIONS OF  
LAW TENDERED BY PLAINTIFFS

The above-entitled action came on regularly for trial on November 26, 1956; November 27, 1956; November 28, 1956, and November 29, 1956, before the Court and a jury duly impaneled and sworn, Honorable O. D. Hamlin, United States District Judge presiding. Max Fink, Esq., and Leon Schiller, Esq., appeared for plaintiffs and Lloyd N. Burke, Esq., United States Attorney, by Lynn J. Gillard, Esq., Assistant United States Attorney, and Marvin D. Morgenstein, Esq., Assistant United States Attorney, appeared for defendant. Oral and documentary evidence was introduced and stipulations were made between respective counsel. The Court granted a directed verdict against the plaintiff, Maurice P. Koch. Pursuant to stipulation, after instructions by the Court, a single interrogatory was submitted to the jury on November 29, 1956, and all

other matters were left to the determination by the Court. The single interrogatory submitted to the jury and the special verdict thereon rendered by the jury is as follows:

“During the year 1947, was H. Koch & Sons regularly engaged in the business of financing motion picture ventures?

Answer: No.”

On the basis of the evidence and stipulations, the Court makes the following:

### Findings of Fact

1. The plaintiffs, Harold M. Koch, William L. Koch, Rebecca Koch Abel and Maurice P. Koch are brothers and sister. The said plaintiffs entered into a partnership pursuant to written agreement on December 31, 1941. and ever since said date have continued as partners under the firm name and style of H. Koch & Sons.

2. The written articles of copartnership of December 31, 1941, provided that the partnership would engage in the business of manufacturing luggage. Said articles of copartnership were amended by written agreement dated October 23, 1944, pursuant to which the partners agreed to also engage in the business of financing motion picture productions. The said partnership agreement, as amended, has remained in full force and effect at all times herein mentioned.

3. The plaintiff, Bessie Koch is the wife of the plaintiff Harold Koch; the plaintiff Rose Koch is

the wife of William L. Koch; and the plaintiff Daisy Koch is the wife of the plaintiff Maurice P. Koch.

4. In 1946 H. Koch & Sons advanced the sum of \$80,000.00 to Beacon Pictures Corporation and the sum of \$10,000.00 to the individual promoters of said Beacon Pictures Corporation, all of which funds were advanced for the promotion and production of a motion picture entitled "Copacabana." Although the entire transaction was conducted as a partnership transaction, the sum of \$15,000.00 of the said sum advanced was especially contributed by the plaintiff Maurice P. Koch for the specific purpose of the said motion picture project and pursuant to the said partnership agreement, as amended, the said Maurice P. Koch was entitled to share proportionately to the extent of the sum of \$75,000.00 contributed by the partnership and entitled to a separate share for the additional funds advanced by him and which were not matched by the remaining partners.

5. Pursuant to written agreements entered into by and between H. Koch & Sons and said Beacon Pictures Corporation it was provided that the sum of \$80,000.00 would be repaid to H. Koch & Sons of and from the proceeds from the distribution and exploitation of the picture "Copacabana" throughout the world, subject to and following the repayment from such proceeds to Bank of America National Trust and Savings Association of the sum of \$730,000.00 and to Standard Capital Company of

the sum of \$277,538.32, and also subject to deduction of the distributors' charges. Pursuant to the said agreement and in consideration of said advance Beacon Pictures Corporation transferred and assigned to H. Koch & Sons, 13 8/10% interest in the said motion picture and in all profits and interests therein.

6. That pursuant to said written agreement between said Beacon Pictures Corporation and H. Koch & Sons it was further provided that in the event the proceeds derived from the sale, distribution and exploitation were insufficient to repay the said \$80,000.00 that said Beacon Pictures Corporation would repay the same in any event.

7. That the sum of \$10,000.00 advanced by H. Koch & Sons to the promoters of the motion picture was advanced pursuant to an agreement wherein and whereby it was provided that the said sum would be repaid only if the project was successful and if the promoters realized profits from their interests in the venture.

8. The motion picture "Copacabana" was not successful and resulted in a loss in the year 1947.

9. During the year 1947, H. Koch & Sons was not regularly engaged in the business of financing motion picture ventures.

10. The partnership of H. Koch & Sons timely filed a partnership income tax return for the year 1947, indicating a net income of \$19,223.19. Thereafter, an amended return was filed indicating a net



loss of \$55,776.82 which resulted from a deduction of the \$75,000.00 loss.

11. Each of the plaintiffs timely filed individual income tax returns for the calendar years 1945 and 1947 with the United States Collector of Internal Revenue for the First District of California. Each of the plaintiffs filed with the same Collector original and amended claims for refund of taxes paid for the years 1945 and 1947 as follows:

	1945		1947	
	Original	Amended	Original	Amended
Harold M. Koch.....	\$ 3,623.90	\$ 3,623.90	\$223.00	\$223.00
Bessie Koch .....	3,673.08	3,673.08	318.00	318.00
William L. Koch.....	3,623.90	3,623.90	223.00	223.00
Rose Koch .....	3,673.08	3,673.08	318.00	318.00
Rebecca Koch Abel....	12,142.17	12,142.17	605.61	605.61
Maurice P. Koch.....	4,649.77	4,649.77	860.62	860.62
Daisy Koch .....	4,797.74	4,797.74	860.53	860.53

The Collector determined and advised each of the plaintiffs of the Collector's determination that the claims for the year 1945 were denied, and that the claims for the year 1947 would be allowed as a non-business bad debt and not otherwise.

12. That the loss sustained by H. Koch & Sons and its respective partners in the year 1947 by reason of the said sums thus advanced resulted from a non-business bad debt.

### Conclusions of Law

1. The loss incurred by H. Koch & Sons in the year 1947 as a result of its investment in the picture "Copacabana" was not a loss incurred in the trade or business of H. Koch & Sons within the

meaning of Section 23(e) of the Internal Revenue Code of 1939.

2. The sums advanced by H. Koch & Sons for the promotion and production of the motion picture "Copacabana" and which became worthless in 1947 was a non-business debt within the meaning of Section 23(k) of the Internal Revenue Code of 1939.

3. The said loss suffered by H. Koch & Sons in the year 1947 is not an allowable deduction in arriving at the net operating loss pursuant to the provisions of Section 122 of the Internal Revenue Code of 1939.

4. The income taxes assessed and collected from plaintiffs by defendant for the years 1947 and 1945 were validly assessed and collected pursuant to the provisions of the Internal Revenue Code of 1939.

5. The defendant the United States of America is entitled to judgment that plaintiffs recover nothing, and that defendant recover its costs incurred.

Dated: December . . , 1956.

.....,

O. D. HAMLIN,

United States District Judge.

Affidavit of Service by Mail attached.

Lodged December 28, 1956.

[Title of District Court and Cause.]

NOTICE OF MOTION FOR  
NEW TRIAL

To the defendant above named and to Lynn J. Gillard and Marvin D. Morgenstein, its attorneys:

Please Take Notice that the undersigned will bring the motion for new trial on for hearing before this Court, in the United States Post Office Building, 7th and Mission Streets, San Francisco, California, on the 21st day of February, 1957, at 9:30 a.m., or as soon thereafter as counsel can be heard.

Dated: February 1, 1957.

LEON SCHILLER,  
MAX FINK,

By /s/ LEON SCHILLER,  
Attorneys for Plaintiffs.

[Title of District Court and Cause.]

MOTION FOR NEW TRIAL

Plaintiffs, Harold M. Koch, Bessie Koch, William L. Koch, Rose Koch, Rebecca Koch Abel, Maurice P. Koch and Daisy Koch, move this Court, Hon. O. D. Hamlin presiding, to set aside the judgment herein and to grant a new trial of the above cause for these reasons:

1. Judgment contrary to law.

2. Judgment contrary to evidence.
3. Evidence is insufficient to support judgment.
4. Error as to admission of evidence.
5. Error as to exclusion of evidence.
6. Verdict not warranted by evidence.
7. Misconduct of counsel for the defendant.
8. Errors in instructions given.
9. Errors in refusal of requested instructions.
10. Errors in findings of fact.
11. Errors in conclusions of law.

Dated: February 1, 1957.

LEON SCHILLER,  
MAX FINK,

By /s/ LEON SCHILLER,  
Attorneys for Plaintiffs.

Receipt of Copy acknowledged.

[Endorsed]: Filed February 1, 1957.

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[Title of District Court and Cause.]

ORDER

Plaintiff's motion for a new trial is denied.

Dated: March 5th, 1957.

/s/ O. D. HAMLIN,  
United States District Judge.

[Endorsed]: Filed March 5, 1957.

**PLAINTIFF'S REQUESTED INSTRUCTIONS**

That it is admitted in this case that H. Koch & Sons is a copartnership consisting of Rebecca Koch Abel, Maurice P. Koch, Harold M. Koch, and William L. Koch.

That it is admitted in this case that the operations of H. Koch & Sons, a copartnership, for the year 1947, resulted in a loss for that year in the sum of \$55,776.82.

Your are further instructed that the amounts advanced by H. Koch & Sons to Beacon Pictures Corporation became bad debts and worthless in the year 1947 and contributed to the over-all loss sustained by H. Koch & Sons.

However, the treatment for income tax purposes of that loss would differ, depending upon whether or not H. Koch & Sons was regularly engaged in 1947 in the business of promoting and financing motion picture ventures.

In order for one to be regularly engaged in the conduct of a particular business, it is not necessary that he devote a major part or any particular part of his time and efforts to such business. Neither is it necessary that he devote a major portion or any particular portion of his capital to such business in order for it to be deemed to be a business regularly carried on by such taxpayer. The amount of time as well as the proportionate amount of capital devoted to a particular business are each factors to be con-

sidered in determining whether or not one is regularly engaged in a particular business.

A taxpayer may engage in or regularly conduct one or several businesses at the same time.

A taxpayer may be deemed to be regularly engaged in the conduct of a particular business even though he may devote most of his time, efforts, and capital to another business or other businesses.

That a trade or business may be regularly carried on by a taxpayer although he does not devote his personal attention to such trade or business. One may conduct a business through employees, agents, representatives and others without devoting one's personal time to such business, and such business may nevertheless be regularly carried on within the meaning of the law applicable to this case.

That taxpayers may act through employees, agents and other persons, firms and corporations appointed by such taxpayers, and that the acts of such employees, agents and other persons, firms and corporations appointed by taxpayers are in contemplation of law the acts of the taxpayers. Thus, in considering the activities of the taxpayers in the instant cause with relationship to the conduct of any business or enterprises, you are required to consider that the acts of any such employees, agents and other persons, firms and corporations appointed by them are in fact the acts and activities of the taxpayers.

The authorized act or acts of any one partner of H. Koch & Sons in connection with partnership busi-

ness or activities are in contemplation of law the act or acts and activities of all the partners.

If the taxpayer regularly and continuously participates in any certain activity then such activity may constitute the trade or business of the taxpayer.

That if you should find that H. Koch & Sons, acting through one or more of its partners, or acting through persons, firms, corporations or representatives appointed by said partnership, has regularly and continuously participated in the promotion and financing of motion picture ventures during the year 1947, then you must find that H. Koch & Sons was engaged in the business of financing and promoting motion picture ventures and that said business was regularly conducted.

The incidence of taxation depends upon the substance of a transaction and not upon the forms utilized by the parties to the transaction. The transaction must be viewed as a whole, and each step, from the commencement of negotiations to the consummation of the transaction, is relevant.

The real facts, not bookkeeping entries, control the determination of taxable income. Account books are evidential but neither indispensable nor conclusive for or against the taxpayer or the government.

That in determining whether or not H. Koch & Sons was engaged in the business of financing motion picture ventures, you must consider, among

other things, the amount of time and effort expended in that direction, and such time and effort, if any, must be considered by you whether or not an actual venture was concluded.

That in considering the activities of H. Koch & Sons with relation to the business of financing motion picture ventures, you must consider all activities designed to advance the financing of such projects and you must consider the same whether or not the transactions were actually concluded.

That in considering the question as to whether or not H. Koch & Sons devoted substantial time to the financing of motion picture ventures, you are required to consider all of their activities relating to that purpose, and all activities and efforts actually expended in attempting to negotiate for and in attempting to enter into financial transactions relating to the business of financing motion picture ventures must be considered by you upon this issue, whether the same were concluded or not.

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## DEFENDANT'S INSTRUCTIONS

The plaintiffs here seek to recover income taxes paid pursuant to the Internal Revenue Laws of the United States. The issue here is the proper treatment of moneys advanced by the plaintiffs to Beacon Pictures Corporation. Plaintiffs seek to deduct the entire amount of this loan in arriving at their net income for the year 1947. To warrant such a deduction of the entire amount of the moneys alleged



to be advanced as a loan, the loan must have been incurred in the plaintiffs' trade or business. The Commissioner of Internal Revenue has determined that the loan was not incurred in the plaintiffs' trade or business.

If a bad debt is not incurred in a trade or business, the taxpayers may deduct it under another section of the Internal Revenue Code. Thus, the plaintiffs in this case would have been allowed a deduction even if you find the plaintiffs were not in the trade or business of promoting and financing motion picture ventures. If the debt is not incurred in a trade or business, the taxpayer is allowed to deduct \$1,000 against his current income, and carry over the amount of the debt which has not been deducted, to each of the next five years.

There is a presumption that the determination by the Commissioner of Internal Revenue that the plaintiffs were not engaged in the trade or business of promoting, organizing, and financing motion pictures is correct, and the plaintiffs have the burden of proving that this determination is wrong.

The burden is on the plaintiffs to overcome the presumption of correctness of the Commissioner's determination, and to prove by a preponderance of evidence that they were engaged in a trade or business of organizing, promoting and financing motion pictures. The preponderance of the evidence means the greater weight of evidence; but this is not determined solely by the greater number of witnesses testifying to any particular fact. The testimony on

~~the part of the party on whom the burden rests must have greater weight in your estimation; have a more convincing effect than that opposed to it.~~

Proof by the taxpayers that they made frequent loans and investments in motion picture ventures is not sufficient to constitute a trade or business. And proof of other attempts to make loans or investments in motion picture ventures is not sufficient evidence for you to find that they regularly engaged in the business of promoting and financing motion picture ventures. Investing and financing is not a trade or business.

Isolated and infrequent promotion and financing of motion pictures is not a trade or business within the meaning of the Internal Revenue Laws. To constitute a trade or business it must be shown that the activity was extensive; it must be shown that the activity was regularly carried on; it must be shown that the activity constituted a substantial portion of the time, energy and effort of those who claim it is a trade or business.

In many instances for taxing purposes the law ignores the existence of a partnership.

United States vs. Coulby,  
251 Fed, 982, 984 (N. D. Ohio), 1918;

Neuberger vs. Commissioner,  
311 U. S. 83, 88 (1940).

Thus, the fact that a partnership was formed to finance motion pictures does not mean that the partners were engaged in the business of promoting

and financing motion pictures. There must exist that great devotion of time and energy by the individual partners to the promotion and financing of motion picture ventures before the taxpayers may claim they were regularly engaged in that business.

The business carried on by a corporation is not to be considered a business carried on by the shareholders, directors or officers. Thus merely because one is an officer, shareholder or director in a corporation which is engaged in the business of promoting and financing motion pictures, does not mean the shareholder or officer or director himself is engaged in the business of promoting and financing motion picture ventures.

There has been testimony of the activity of Maurice P. Koch as shareholder, officer and director of Producers Finance Corporation. I instruct you that the conduct of Maurice P. Koch in furtherance of the promotion and financing of motion picture ventures on behalf of Producers Finance Corporation may not be considered by you in determining whether any of the plaintiffs were engaged in the business of promoting and financing motion picture ventures if you believe Maurice P. Koch was acting in his capacity as a corporate officer, shareholder and director.

Defendant has put in issue the question of whether Maurice P. Koch individually loaned \$15,000 to Beacon Pictures Corporation. This issue is distinct from the question raised by the other interrogatories submitted to you. Accordingly, your answer to the

question of whether this money was loaned by Maurice P. Koch may differ with your answers to the other interrogatories.

Maurice P. Koch has alleged in the complaint that he individually loaned \$15,000 to Beacon Pictures Corporation in excess of the amount loaned by the Partnership of Koch & Sons. The complaint is not evidence in the case, nor are any allegations in the complaint evidence in this case. Thus, the burden still rests on Maurice P. Koch to prove by a preponderance of the evidence that individually he loaned \$15,000 to Beacon Pictures Corporation.

Counsel have a right, and indeed a duty, to argue the case to you. It is your duty to listen and to be attentive, and to give weight and consideration to the arguments of the counsel. However, in their comments upon the facts of the case, if you find that there is any discrepancy between what they stated to you to be the facts of the case and the words that have come from the mouths of the witnesses, you must disregard, if there is such conflict, the statement as to the facts made by the attorneys, and consider only the evidence given by the witnesses in that regard.

You are the sole judges of the credibility of each witness, and it is for you to pass on the reliability of each witness.

In determining the credibility of a witness, you may consider his interest in the outcome of the trial.

If you believe that Maurice P. Koch used his own money in any transaction, and was acting therein in his own behalf and not in behalf of H. Koch & Sons, that transaction is to be considered only in determining whether Maurice P. Koch was engaged in the business of financing motion picture ventures and can not be considered by you in determining whether the partnership of H. Koch & Sons was engaged in the business of financing motion picture ventures.

The burden of proof in this case is upon the plaintiffs to prove by a preponderance of the evidence that the loan by plaintiffs to Beacon Picture Corporation was a loan made in plaintiffs regular trade or business. ~~By preponderance of the evidence is~~ meant the greater weight of evidence, and if you find that the evidence is equal on both sides, then you should find for the defendant. You are further instructed that an income tax deduction is a matter of legislative grace and that the burden of clearly showing the right to the claimed deduction is on the ~~plaintiffs.~~

In considering the testimony of each witness in this case you should take into consideration the interest of the witnesses, if any, who have testified, the manner in which they have given their testimony, their candor or lack of candor, their frankness or lack of frankness, the reasonableness or unreasonableness of their statements or opinions, and from all these facts and circumstances, together with all the other facts and circumstances in the

case, determine whether or not the loan in question was made as a part of plaintiffs' trade or business.

That the term "trade or business" as used in Sec. 23(e) of the Internal Revenue Code of 1939 does not encompass all activities engaged in for a profit. By "trade or business" is meant that trade or business which is regularly engaged in by plaintiffs and does not include occasional or isolated transactions entered into for profit.

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[Title of District Court and Cause.]

### NOTICE OF APPEAL

Notice Is Hereby Given that Harold M. Koch, Bessie Koch, William L. Koch, Rose Koch, Rebecca Koch Abel, Maurice P. Koch and Daisy Koch, plaintiffs above named, hereby appeal to the United States Court of Appeals for the Ninth Circuit, from the final judgment entered in this action on January 23, 1957.

Dated: April 18, 1957.

MAX FINK,  
LEON SCHILLER,

By /s/ LEON SCHILLER,  
Attorneys for Plaintiffs.

[Endorsed]: Filed April 18, 1957.

The United States District Court Northern District  
of California, Southern Division

No. 34,762

HAROLD M. KOCH, BESSIE KOCH, WILLIAM  
L. KOCH, ROSE KOCH, REBECCA KOCH  
ABEL, MAURICE P. KOCH and DAISY  
KOCH,

Plaintiffs,

vs.

UNITED STATES OF AMERICA,

Defendant.

Before: Hon. O. D. Hamlin, Judge.

TRANSCRIPT OF TRIAL

November 26, 1956

Appearances:

For the Plaintiffs:

MAX FINK, ESQ., and  
LEON SCHILLER, ESQ.

For the Defendant:

LLOYD H. BURKE, ESQ.,  
United States Attorney, by  
LYNN J. GILLARD, ESQ.,  
Assistant U. S. Attorney.

(A jury of twelve persons was duly im-  
paneled and sworn to try the cause.)

(Opening statements were made by counsel for the respective parties.)

The Court: Call your first witness.

Mr. Schiller: We will call Mr. Maurice P. Koch.

### MAURICE P. KOCH

one of the plaintiffs, was called as a witness in his own behalf, and after being first duly sworn, testified as follows:

#### Direct Examination

By Mr. Fink:

Q. Mr. Koch, will you state your full name, please? A. Maurice P. Koch.

Q. Do you have a brother named Harold M. Koch? A. Yes, sir.

Q. Do you have a brother named William L. Koch? A. Yes.

Q. A sister named Rebecca Koch?

A. That is right.

Q. Your sister, Rebecca, has been married since this action was started, or prior to the starting of this action—I will withdraw the question.

Your sister, Rebecca Koch, has been married in the past few years? A. That is right.

Q. What is her name now?

A. Rebecca Abel. [4\*]

Q. Are you and your brothers and your sister engaged in business? A. Yes.

Q. As a partnership? A. That is right.

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\*Page numbering appearing at top of page of original Reporter's Transcript of Record.



(Testimony of Maurice P. Koch.)

Q. When was this partnership first started?

A. Started in 1941.

Q. Mr. Koch, I show you here a document which bears the date of December 31, 1941, and seems to bear the signatures of Maurice Koch, Rebecca Koch, Harold Koch, and William L. Koch. Are these the signatures of yourself, your two brothers and your sister that you just mentioned? A. They are.

Q. Is this your partnership agreement?

A. That is right.

Mr. Fink: May I have this marked as plaintiffs' 1 in evidence, your Honor?

Mr. Gillard: No objection.

The Court: It may be so marked.

(The partnership agreement referred to was marked Plaintiffs' Exhibit No. 1 in evidence.)

Q. (By Mr. Fink): I will show you here, Mr. Koch, a document which bears date the 23rd day of October, 1944, between the same parties, and it is called "Amendment to Agreement of December 31, 1941." Is this the amendment to the document [5] that has just been marked Exhibit 1?

A. That is right.

Q. And also the four signatures, "Rebecca Koch, Maurice Koch, Harold M. Koch, and William L. Koch," are these the signatures of yourself, your brothers and your sister? A. They are.

Mr. Fink: May we offer this as Exhibit 2, your Honor?

Mr. Gillard: No objection.

(Testimony of Maurice P. Koch.)

The Court: It may be so marked.

(The amendment to agreement referred to was marked Plaintiffs' Exhibit No. 2 in evidence.)

Q. (By Mr. Fink): Mr. Koch, I show you here a document which is called "Agreement of Partnership," and bears date the 23rd day of October, 1944, which I want to point out to you is the same date which appears on the document, Exhibit 2, which you just saw. This seems to be the agreement of partnership of Producers Syndicate.

A. That is right.

Q. Do you recall this document?

A. Yes, sir.

Q. Have you observed the signatures that appear on this document?           A. Yes.

Q. Are you familiar with some of them?

A. All of them. [6]

Q. With all of them?           A. Yes, sir.

Mr. Fink: We will offer this as Plaintiffs' Exhibit 3, your Honor—Agreement of Partnership of Producers Syndicate, October 23, 1944.

Mr. Gillard: I will object to that as being incompetent, irrelevant and immaterial and having no bearing upon the issues of this case. If the Court will permit me to take the witness on voir dire for the moment I will appreciate that. This is the situation which Mr. Fink referred to in his opening statement, in which no investment resulted, and as such it is our position that it has no bearing upon

(Testimony of Maurice P. Koch.)

the issues of the case. It does not show whether or not the plaintiffs were or were not in the business of financing motion picture production.

Mr. Fink: Your Honor, our position on that is that \$50,000 was invested. It ties in with the partnership agreement which was amended on that same date to permit this type of activity to go into the motion picture financing business.

The Court: It may be admitted and marked Plaintiffs' Exhibit 3, subject to a motion to strike.

(The agreement of partnership referred to was marked Plaintiffs' Exhibit No. 3.)

Q. (By Mr. Fink): Mr. Koch, did you know a Mr. David Hersh? A. Yes, sir. [7]

Q. Did you know a Mr. Sam Coslow?

A. Yes, sir.

Q. Did you know a Mr. David Sebastian?

A. Yes.

Q. How long have you known Mr. Sebastian?

A. Over 30 years.

Q. Is he related to you by marriage?

A. That is right.

Q. What is his relationship to you?

A. My brother-in-law.

Q. Mr. Hersh—when did you first meet him?

A. I met Mr. Hersh in the early part of 1946.

Q. What was the occasion of your meeting with Mr. Hersh?

A. I met Mr. Hersh—was brought to me relative to picture deals.

(Testimony of Maurice P. Koch.)

Q. Where did you meet Mr. Hersh?

A. I met Mr. Hersh—the first time I met Mr. Hersh was in Los Angeles.

Q. The Hollywood area there?

A. That is right.

The Court: What was his first name, please?

A. His first name was—I just can't think of it right now.

Mr. Fink: May I suggest the name? The witness seems to be confused.

Q. Was that David Hersh? [8]

A. David Hersh, that is right.

Q. You met him, you say, in Hollywood early in 1946?

A. That is right.

Q. Did you have discussions with him?

A. Yes, we discussed the——

Q. Just a moment, please. Did you also have discussions with Mr. Coslow?

A. That is right.

Q. Did you also have discussions with Mr. Sebastian at that time?

A. Yes.

Q. Were these discussions held jointly or separately with each of these gentlemen?

A. Well, they were held jointly and I talked to each one of them in the room there.

Q. Approximately on how many occasions in the early part of 1946 did you see Mr. Hersh?

A. I saw Mr. Hersh several times. He would come up to San Francisco and I would visit with him in Los Angeles.

Q. Did you have telephone conversations with him, also?

A. Yes.

(Testimony of Maurice P. Koch.)

Q. In your early discussions with Mr. Hersh what was the subject of your discussion?

A. The subject of the discussion was producing—promoting, rather, and financing a pre-production money on motion pictures. [9] We were going to——

Q. Tell us for a moment in a little more detail just what you mean by that.

A. We talked about making a lot of pictures. Mr. Hersh at that particular time was working for Ideal Factors in New York, and Mr. Hersh was in the business of loaning secondary money completion money to pictures that had already received bank money and pre-production money, and he had produced one, two, or three pictures himself.

We discussed going into the promotion and financing of motion pictures. We were going to make some big pictures and some B pictures.

Q. What part were you to play in this? What was your contribution toward the production of pictures going to be?

A. We were going to——

Mr. Gillard: I will object to the form of the question as calling for the opinion and conclusion of the witness.

The Court: Sustained.

Mr. Fink: I will reframe the question, your Honor. I recognize this is all generally hearsay. However, the question is directed——

The Court: There is no need to discuss it, Counsel. Ask your next question. The objection is sustained.

(Testimony of Maurice P. Koch.)

Q. (By Mr. Fink): Mr. Koch, was there any discussion that you engaged in at that time with regard to the details of your [10] participation or activity in such a venture?

A. Yes; Mr. Hersh had told me about Sam Coslow. He was a very good friend of Mary Pickford's. Mary Pickford had arranged to give Sam Coslow three releases through United Artists. At that particular time releases were almost impossible to get.

So we decided to form a combine whereby we could use Sam Coslow's releases and we would put up the pre-production money, and Hersh would get the bank money and the secondary money from Standard Capital and start this first picture rolling, and at the turn of the camera we would recoup this pre-production money from the bank money and start the second picture rolling.

Q. Did these discussions occur over several different conversations and visits?

A. Yes, we had a lot of meetings.

Q. Have you given us the substance of the conversations that occurred in these meetings up to this particular point?

A. Well, the most important substance was that we were going to put up the money for the pre-production, and we were going to have something to say as to how the money was used in the pre-production, and Hersh and Sebastian were going to form a partnership to watch over all of these things for me. We were going into this—we found this story, "Copacabana," that we were going into. We also

(Testimony of Maurice P. Koch.)

discussed the participation that we [11] would receive——

Mr. Gillard: Just a minute. Is this a continuation of the same answer?

Is there a question pending of the witness?

Mr. Fink: The last statement may go out.

The Court: Very well.

Q. (By Mr. Fink): Mr. Koch, I show you here a document between Copacabana, Inc., as owner and producer, the name being left blank as to who the producer is. It bears date of April 8, 1946. It appears to be signed by Copacabana, Inc., by Monte Proser as president, Beacon Pictures, Inc., by George Frank, secretary. Are you familiar with this document?

A. Yes, sir. That grants him the right to the name "Copacabana," and the story.

Mr. Fink: The document will speak for itself.

May we offer this, your Honor, as Plaintiffs' Exhibit 4?

Mr. Gillard: I object to that as incompetent, irrelevant and immaterial, having no bearing on the question of the plaintiffs' activities in this case. This is an agreement between two third persons.

The Court: It is time to take the recess at this time. We will take a recess until 2:00 p.m., and I will have an opportunity to look at that at 2:00 o'clock this afternoon.

(Whereupon, a recess was taken until 2:00 o'clock p.m.) [12]

Monday, November 26, 1956, 2:00 P.M.

The Court: Before the recess you offered this document dated April 8, 1946. It may be received in evidence subject to a motion to strike if it is not connected up.

(The Copacabana rights agreement referred to was marked Plaintiff's Exhibit No. 4 in evidence.)

MAURICE P. KOCH

one of the plaintiffs, a witness in his own behalf, on the stand at the time of recess, having been previously duly sworn, resumed the stand and testified further as follows:

Direct Examination

(Resumed)

By Mr. Fink:

Q. Mr. Koch, you told us this morning about your discussions with regard to setting up an operation to finance independent producers and participate in the so-called preproduction or promotion of pictures. Did you discuss this venture and this plan with your brothers, who were your partners, and your sister?

A. Yes. We went through this quite thoroughly, even at the beginning of all these ventures.

Q. Can you tell us whether or not they likewise had discussions with Mr. Hersh?

A. They talked to Mr. Hersh when he was in San Francisco, and he talked to my brothers and sister.



(Testimony of Maurice P. Koch.)

Q. Did they likewise have discussions, to your knowledge, [13] on that subject with Mr. Sebastian?

A. They talked with Mr. Sebastian, too, quite frequently.

The Court: When you say "they," who do you mean?

A. I mean Mr. Sebastian talked to my sister and my brothers quite frequently on these picture deals.

Q. (By Mr. Fink): About this plan?

A. Yes.

Q. And about these ventures?

A. That is right.

Q. Did H. Koch and Sons have legal counsel in San Francisco?      A. Yes, sir.

Q. Who was the attorney for your partnership?

A. Morris M. Grupp.

Q. Do you know whether or not Mr. Grupp did anything on behalf of the partnership and as counsel for the partnership in connection with this plan of picture ventures?

A. Well, Mr. Grupp sat in with Hersh and Sebastian when they came up here talking about these picture deals, and myself.

Q. Who was Mr. Grupp acting for in that regard?

A. Mr. Grupp was acting in my behalf?

Q. When you say your behalf you mean you, personally?

A. No; for the firm of H. Koch and Sons.

(Testimony of Maurice P. Koch.)

Q. By the way, in this firm of H. Koch and Sons, do you have a brother, Harold?

A. Yes. [14]

Q. Generally, since the year 1941, what have been his activities in that business?

A. My brother, Harold, has been the plant manager. He has run the factory.

Q. Did he actually do labor in the plant?

A. Yes, he did labor in the plant, and ran the factory.

Q. Going back to the year 1941, when you first started your business—and I assume it was a great deal smaller at that time than it is now——

A. That is correct.

Q. ——what were his duties at that time?

A. His duties were to—well, he would receive the orders, make up cutting tickets, and supervise the entire plant, and supervise the merchandise going through the plant.

Q. Your brother, William, what did he do?

A. He assisted my brother, Harold.

Q. What did your sister do?

A. My sister was in charge of the books.

Q. She is referred to by the name of “Beck”?

A. “Beck,” that is right.

Q. Her name is Rebecca?

A. Rebecca Koch Abel, yes.

Q. She took care of the bookkeeping?

A. That is right.

Q. She ran the office, more or less? [15]

A. That is right.

(Testimony of Maurice P. Koch.)

Q. What did you do?

A. I was the general manager of the plant. I took care of the financing of the business, took care of bank loans, took care of the buying and the selling of merchandise, took care of most everything that went in and out of the place.

Q. Were you referred to by any title?

A. No. I was the general manager—what you would call the boss of the business.

Q. Has that same arrangement continued ever since the time that you, your brothers and your sister took over this business in 1941?

A. Yes.

Q. It had previously been your father's business?

A. That is correct.

Q. You mentioned this morning that a man named Sam Coslow had an arrangement with United Artists, Mr. Koch.

A. That is right.

Q. I show you here a document which bears date of April 16, 1946, which purports to be a contract between Sam Coslow and United Artists Corporation. Have you had occasion to see this document?

A. Yes.

Q. You have made a study of it, have you?

A. Not recently. [16]

Q. But you have seen it?

A. Yes, I was very much interested in that in 1946.

Q. Could you recognize the signature of Sam Coslow?

A. It does look like his signature?

(Testimony of Maurice P. Koch.)

Mr. Fink: I will offer this document as plaintiffs' next in order, your Honor. It purports to be an agreement between Sam Coslow and the United Artists Corporation dated April 16, 1946. It generally provides for the distribution of the films throughout the world.

Mr. Gillard: I object to it, if your Honor please, on the ground that no foundation has been laid for the introduction of it in evidence.

The Court: I do not see the foundation.

Mr. Fink: May I have it marked at this time plaintiffs' next in order?

The Court: Exhibit 5 for identification.

(The agreement referred to was marked Plaintiffs' Exhibit No. 5 for identification.)

Mr. Fink: I will seek to identify the signatures by a later witness in this case, your Honor.

Q. I think you told us this morning that the first of these films, in 1946, in which you intended to participate in the preproduction matters was a picture called Copacabana. Can you tell us whether or not a corporation was organized with respect to that picture? [17]

A. Well, a corporation was subsequently organized for that picture.

Q. What was the name of that corporation?

A. Beacon Pictures Corporation.

Q. Were you an officer of that corporation?

A. No, sir.

(Testimony of Maurice P. Koch.)

Q. Did you ever receive any salary from that corporation for your personal efforts?

A. No, sir.

Q. I show you here what purports to be a photostat of a check of April 25, 1946. It purports to have been drawn by H. Koch and Sons to the order of David Sebastian. Is this your signature and is that in your handwriting?

A. Yes, sir.

Q. On the reverse side it purports to bear the endorsement of David Sebastian and Dave Sebastian. Are those his signatures?

A. Those are his signatures.

Mr. Fink: May I offer this as plaintiff's next in order?

Mr. Gillard: No objection.

The Court: Exhibit 6.

(The photostatic copy of the check referred to was marked Plaintiffs' Exhibit No. 6 in evidence.)

Mr. Fink: Perhaps we should note for the record, your Honor, that by stipulation between counsel it has been agreed [18] that photostats may be used with the same force and effect as originals throughout this cause, unless particular objection is made.

Is that so stipulated?

Mr. Gillard: With reference to those documents I have seen photostats of prior to this time, yes, Mr. Fink.

(Testimony of Maurice P. Koch.)

The Court: Who do you contend is the maker of this check, counsel?

Mr. Fink: The maker of the check, your Honor, is H. Koch and Sons.

The Court: It appears to be on the personal check of Maurice P. Koch. It appears also to have the personal signature of Maurice P. Koch. That is the reason I asked the question. It does not appear to be a check of Koch and Sons on the printed portion of it.

Mr. Fink: Your Honor, the check appears to be a blank check of Maurice P. Koch, one of his blank forms with his name printed on it. However, the signature reads "H. Koch and Sons," and it is signed by Mr. Koch as a partner.

The Court: It doesn't say "By Maurice Koch." There is no "By" there, is there?

The Witness: May I explain that, your Honor?

The Court: Ask the witness. The check, itself, does not indicate what you say it does.

Q. (By Mr. Fink): Mr. Koch, I show you this check of April [19] 25, 1946. Upon whose bank account was that check drawn?

A. It was drawn on the account of H. Koch and Sons.

Q. Who made out the check?

A. I made out the check.

Q. I see that you did not use a regular partnership check form for it. A. That is right.

Q. You wrote in the "H. Koch and Sons."

A. Yes, sir. May I explain this, Mr. Fink?

(Testimony of Maurice P. Koch.)

Q. Yes.

A. I made out a lot of checks like this, your Honor. I am in a place where I do not have a firm check with me, and the bank will honor any check. As a matter of fact, our checks are all printed this way, "H. Koch and Sons," on the bottom, irrespective of what is above the check. As long as the signature of the check appears with H. Koch and Sons, and my signature below the H. Koch and Sons, that would be a firm check and would be withdrawn from the account of H. Koch and Sons.

The Court: Don't you write "By"?

A. No, sir, not on any check, no, sir; it isn't necessary.

Q. Do you ordinarily use your personal check to make a check upon the firm funds?

A. Only when I am in a deal where I might be at a luncheon in Los Angeles, and we are sitting there, and I have to write [20] a check, I will use my own check, my own personal check, a counter check, or a blank check. I have done that on very many occasions. And the bank has honored all these checks with my signature underneath the firm name of H. Koch and Sons. It doesn't have to be a printed check. And this check is legal tender, a legal check.

Mr. Fink: If your Honor please, may I at this time, since there has been discussion about the check, pass the check to the jury to view at this time?

The Court: You may.

(Testimony of Maurice P. Koch.)

Proceed with your next question, Counsel.

Q. (By Mr. Fink): Mr. Koch, what was that check for, the \$15,000 represented by that check? What was it for?

Mr. Gillard: I object to that as calling for the opinion and conclusion of the witness.

The Court: I think he may answer for what purpose he gave it.

A. That check was an advancement to Dave Sebastian for the purpose of setting up the corporation of Beacon Pictures Corporation, **relative to** Hersh and Coslow's interest in that corporation, and \$5,000—\$10,000 of that check was for that purpose. The other \$5,000 was an advancement to the Hersh and Sebastian partnership for expenses to carry on the show and to **get things going and rolling** on this particular picture. All those moneys were to come back to us—— [21]

Q. (By Mr. Fink): Just what they were for, is the question. A. Yes.

Q. You say \$10,000 was to get the corporation started—Beacon Pictures Corporation. Is that the one you have reference to?

A. That is right.

Q. And \$5,000 was for what?

A. To get the picture going, for expenses—the “Copacabana” picture.

Q. Had there been any picture, at that time, made?

A. No, sir. This was part of the pre-production money, or for preproduction.



(Testimony of Maurice P. Koch.)

Mr. Gillard: I ask that that go out as the opinion and conclusion of the witness, and move to strike it out. He has testified it went to Hersh and Sebastian.

The Court: The latter part may be stricken.

Q. (By Mr. Fink): I show you here what purports to be a letter of May 17, 1946, or a receipt. It purports to bear the signature of David Hersh. Do you recognize Mr. Hersh's signature?

A. Yes.

Q. That is his signature?

A. That appears to be, yes.

Mr. Fink: We will offer that as plaintiffs' next in order, your Honor. [22]

Mr. Gillard: No objection.

The Court: Exhibit 7.

(The letter-receipt referred to was marked Plaintiffs' Exhibit No. 7 in evidence.)

Mr. Fink: I was wondering, your Honor, if it might be helpful to read this into the record at this time.

The Court: It is in evidence and the jury can see it, and will see it, at such time as may be proper. I think it would only encumber the record by reading it in there. It is already in evidence. Do you desire to question the witness about the letter?

Mr. Fink: Not at this time, your Honor.

The Court: If you do not, I do, Counsel, to get something clear in my mind.

Q. You stated of the \$15,000 that was mentioned

(Testimony of Maurice P. Koch.)

in this check dated April 25, 1946, that \$10,000 was to be used by David Sebastian.

A. \$10,000 was to be used by Hersh and Coslow in the forming of the corporation.

Q. For what? What was it to be for?

A. The corporation was to be the vehicle by which they would transact all the business of "Copacabana."

Q. Were you making a gift of this \$15,000?

A. No, sir.

Q. What did you get for it? [23]

A. Well, when the corporation was dissolved, I was to receive my \$10,000.00 back from Hersh and Coslow, plus a part of their percentage of the picture.

Q. You were to get a percentage of the profits of the picture, were you? A. That is right.

Q. In this letter of May 17, 1946, the opening sentence says, "I hereby acknowledge receipt from you of your check in the sum of \$10,000.00." Is that the \$10,000.00 that you say was represented by a portion of this check? A. Yes, sir.

Q. It then goes on to say, "You are delivering your check to me to be utilized for the purpose of purchasing 40 per cent of the stock of Beacon Pictures Corporation?"

A. That is right.

Q. That was the purpose of the money then?

A. That is right.

Q. (By Mr. Fink): Did you, Mr. Koch, expend other moneys for the expenditures incurred by Se-

(Testimony of Maurice P. Koch.)

bastian and Hersh in the putting together or promotion of this motion picture "Copacabana," that is, funds in addition to the \$15,000.00?

A. Yes, there is another check of \$2,500.00 that went into Hersh and Sebastian.

Mr. Fink: May the record show that all the documents which I have exhibited to the witness have been previously [24] exhibited to counsel for the government, your Honor.

The Witness: That is the check, yes, sir.

Q. (By Mr. Fink): Do you recognize this check? A. That is right.

Q. This is your signature?

A. That is right.

Q. Whose account is this check drawn on?

A. H. Koch & Sons.

Mr. Fink: May we offer this as plaintiff's next in order, your Honor?

The Court: No. 8.

(The check referred to was thereupon received in evidence and marked Plaintiffs' Exhibit 8.)

Q. (By Mr. Fink): Mr. Koch, this transaction that we have been discussing occurred in the year 1946, a little over 10 years ago. Do you purport at this time, 10 years later, to have all the documents, all the memorandums involved in this transaction?

A. I can't say that I have all of them.

Q. You do have some of them?

(Testimony of Maurice P. Koch.)

A. That is right, sir.

Mr. Fink: Your Honor, with regard to the next exhibit that I intend to show to the witness, which is a letter dated July 31, 1946, addressed by the witness to David Hersh, we have both the copy, which I represent was taken from the [25] witness' files, as well as the original letter which was sent out. Counsel has stipulated with me that the original letter was taken from the files of Beacon Pictures, and it was received by Mr. Hersh in Los Angeles, is that correct, counsel?

Mr. Gillard: That is correct.

Q. (By Mr. Fink): Mr. Koch, I will show you a letter of July 31, 1946, on the letterhead of H. Koch & Sons. It purports to be your signature.

A. That is right.

Q. Did you write this letter?

A. Yes, sir.

Q. You sent it to Mr. Hersh?

A. Yes.

Mr. Fink: I offer this as plaintiffs' next in order, your Honor.

Mr. Gillard: No objection.

The Court: Exhibit No. 9.

(The letter referred to was thereupon received in evidence and marked Plaintiffs' Exhibit 9.)

Q. (By Mr. Fink): I will show you here a telegram addressed to Maurie P. Koch and purporting to be sent by David Hersh. Did you receive

(Testimony of Maurice P. Koch.)

this telegram?           A. That is right.

Mr. Fink: May I offer this in evidence as plaintiffs' next in order? [26]

Mr. Gillard: No objection.

The Court: Exhibit 10.

(The telegram referred to was thereupon received in evidence and marked Plaintiffs' Exhibit 10.)

Q. (By Mr. Fink): I show you here a photostat of a check of August 5, 1946, on the account of H. Koch & Sons for \$50,000. It purports to bear the signature of Rebecca Koch on behalf of H. Koch & Sons. Is that your sister, a partner's signature?           A. That is right.

Mr. Fink: I offer that as plaintiffs' next in order, your Honor.

Mr. Gillard: No objection.

The Court: Exhibit 11.

(The document referred to was thereupon received in evidence and marked Plaintiffs' Exhibit 10-A.)

The Court: To get these three documents to the attention of the jury, perhaps it would be better if you read the letter and the check and the telegram.

Mr. Fink: If I may, your Honor. Exhibit 9. Letter on the stationery of H. Koch & Sons, 73 Beale Street, San Francisco 5, addressed to David Hersh, c/o Goldwyn Studios, 1421 North Formosa Avenue, Los Angeles, California.

(Testimony of Maurice P. Koch.)

“Dear Dave:

“Dave informed me of the conversation he had with you last evening relative to the participation I am to receive [27] for the loan of certain monies to you both for use in Copacabana.

“Subsequent to the above conversation when you were up here we had agreed that I was to receive in addition to the payment of the loan one and a half to two per cent for each unit of ten thousand dollars I advanced to you both. Since you have expressed yourself with a statement to Sebastian that one and a half per cent for each ten thousand dollars advanced is the best that you can do, I must likewise, in all fairness to my people express myself. I am not asking you to compromise with me as I did with you. All I am asking for is what we originally agreed upon. Because of the arithmetic of money versus participation the one and a half per cent should be straight across. So far I have advanced to Hersh and Sebastian \$17,500.00. Of this sum Hersh and Sebastian partnership advanced to Hersh individually and Caslow individually the total sum of \$10,000.000 which they used as their contribution to Beacon Pictures, Inc. The \$7,500.00 remaining is still intact in your partnership firm account. Therefore, any participation I shall receive should be handled as follows:

“For all monies hereafter loaned to you, including the \$7,500.00 in your possession, I should receive one and one half per cent participation for

(Testimony of Maurice P. Koch.)

each \$10,000.00 unit [25] advanced, direct from United Artists, the distributor.

“On the other hand in return for the ten thousand dollars originally put up for you and Caslow I am perfectly willing to have you work out an equivalent percentage to be paid by Hersh-Sebastian partnership.

“Please let me hear from you immediately on the above. Also incorporate in the document drawn in Grupp’s office the terms mutually agreed upon and forward same to me.

“Mr. Grupp also advises me that since the security to protect any advances is not now in existence that it should be understood that I need not rely on such security but may waive the same at any time I so desire. Such waiver, however, to be in writing signed by me.

“With kindest regards, I am

“Sincerely,

“(S) MAURICE P. KOCH,

“(T) MAURICE P. KOCH.”

Mr. Fink: May I, at this time, question this witness about this document, your Honor?

The Court: You may.

Q. (By Mr. Fink): Mr. Koch, to us laymen some of these terms are not clear and I want to ask you about them. The letter says, among other things, “I must likewise in all fairness to my people express myself.” To whom do you refer when you say “my people”? [29]

A. My partners.

(Testimony of Maurice P. Koch.)

Q. You used the word "participation." What do you mean by the use of that word "participation"?

A. That is any participation in the picture, percentages of the picture with them. I was to receive certain percentages along with them for my advancement to them of the moneys.

Mr. Gillard: I move that the answer go out, if the Court please, on the ground that the definition the witness is now trying to place upon the term "participation" is inconsistent with the document itself.

The Court: The answer may remain.

Q. (By Mr. Fink): When you say here, "I should receive one and one half per cent participation for each \$10,000.00 unit advanced direct from United Artists, the distributor," what do you mean by that?

A. I felt that when United Artists would distribute the moneys, after they received moneys from the picture houses, they would have all these moneys and then distribute them to Beacon Pictures, and that they should distribute my money to me direct instead of to Beacon.

The Court: Does that mean in gross receipts?

A. That is receipts after they had deducted—that would be receipts after they had deducted their, I believe, 27 per cent for distribution. They received so much for distribution of a picture and the balance of the moneys are sent back to the [30] corporation itself that owned the picture.



(Testimony of Maurice P. Koch.)

Mr. Fink: Turning to this telegram, which appears to be a night letter with a deadline of Los Angeles, California, addressed to Murray P. Koch, Personal, care Koch and Son, 73 Beale Street, San Francisco, August 4, 1946, it reads,

"Kindly instruct David Sebastian return immediately. He bring 50,000. Will not give Beacon until properly secured. David talk Weintraub satisfies me everything will be OK. Please have utmost confidence our management and fairness to you. Will complete whatever necessary Davids return. Kindest regards. David Hersh."

Turning to Exhibit 11, it is a check this time on the firm checks that states, "Koch and Sons," signed "H. Koch and Sons." Underneath that, "Rebecca Koch," dated August 5, 1946, "Pay to the order of David A. Sebastian \$50,000.00, the sum of \$50,000.00 drawn on Pacific National Bank of San Francisco, San Francisco, California," and in the upper left-hand corner the voucher, which is part of the check, there appear these words: "8/5. In line with understandings arrived at re Copacabana picture."

Mr. Gillard: Is this in evidence, counsel?

Mr. Fink: Yes, it is Exhibit 11. The photostat of the reverse side of the check shows "Deposit to the account of Hersh and Sebastian and David A. Sebastian."

Q. By the way, at or about the time of that \$50,000.00 check, [31] or shortly thereafter, did you participate in negotiations for other picture deals?

(Testimony of Maurice P. Koch.)

A. Yes, we were——

The Court: Just answer the question.

The Witness: Yes.

Q. (By Mr. Fink): Can you tell us approximately how many different deals were looked into by you over the period of the last six months of 1946?

Mr. Gillard: I object to that as vague and speculative, and calling for the opinion and conclusion of the witness.

The Court: I think in view of the objection he would have to give the individual contacts.

Q. (By Mr. Fink): I show you here a letter on the letterhead of Beacon Pictures, signed Charles Weintraub, of September 9, 1946, and ask you if you are familiar with that letter. A. Yes.

Q. Do you know Charles Weintraub?

A. Yes, I do

Q. How long have you known him?

A. I have known Charles Weintraub for about 25 or 26 years.

Q. Do you recognize his signature?

A. Yes.

Q. This letter has attached to it a document which purports to be a typewritten memo of August 6, 1946. Did this matter come to your attention? [32]

A. Yes, sir, with a lot of other matters.

Mr. Fink: I offer this as plaintiffs' next in order, your Honor.

Mr. Gillard: I will object to this as being incompetent and immaterial, concerning the activities

(Testimony of Maurice P. Koch.)

of the Beacon Pictures Corporation, which has nothing to do with this individual, who is not even a stockholder or director of that corporation, and even if he were a stockholder or director, the business of the corporation would not be his business as an individual, as a partner of H. Koch & Sons.

Mr. Fink: I would have some additional questions to ask the witness on this subject, your Honor, in view of the objection counsel has made.

Q. Mr. Koch, will you tell us whether or not there was ever any discussions to the effect that a picture deal called the "Long November" would ever be a part of the Beacon Picture setup?

Mr. Gillard: Objected to as incompetent, irrelevant and immaterial. That corporation's business is not the business of this individual.

The Court: The objection may be sustained.

Q. (By Mr. Fink): Mr. Koch, on or about the year 1946 and the year 1947, which is in question in this trial, were you familiar with the practice which generally prevailed in the independent picture business with regard to the use of [33] corporations?

Mr. Gillard: I object to that as incompetent, irrelevant and immaterial.

The Court: The objection may be sustained.

Q. (By Mr. Fink): Can you tell us, Mr. Koch, whether or not the picture or the proposed picture, "The Long November," whether that had anything to do with Beacon Pictures Corporation?

Mr. Gillard: I object to that as incompetent, irrelevant and immaterial.

(Testimony of Maurice P. Koch.)

The Court: I will permit him to answer that.

The Witness: That was——

The Court: Just answer the question.

Mr. Fink: Did it have anything to do with Beacon Pictures?

A. Some of the people in Beacon Pictures.

Q. You mean some of the same people were in "The Long November" deal who were in the Beacon Pictures deal? A. That is right, sir.

Q. Did the deal "The Long November," was it ever planned for Beacon Pictures Corporation or was it planned for some other setup?

A. That was planned for some other setup.

Mr. Fink: We would like to offer the exhibit, your Honor, that pertains to this "Long November" transaction merely to show the activity at that time. [34]

Mr. Gillard: If your Honor please, I will renew my objection. The idea of trying to prove that this taxpayer was involved in the business of financing motion picture productions by virtue of the activities of everybody else in Hollywood with reference to other matters is not a relevant subject for us to go into.

The Court: The objection may be sustained.

Q. (By Mr. Fink): Let us put it this way, Mr. Koch: In the year 1946, how much of your time did you devote to the promotion and financing of motion picture ventures?

A. About a third of my time.

(Testimony of Maurice P. Koch.)

Q. On how many occasions did you go to Hollywood?      A. Oh, innumerable occasions.

Q. What was the longest period of time you stayed there at any one stretch solely for picture work?      A. A little better than three weeks.

Q. When was that?

A. That was in 1946, the latter part of 1946.

Q. Do you recall when the actual production, that is, the actual photography of the picture "Copacabana" started?

A. It was the latter part of 1946. I can't tell you exactly.

Q. Were you there at the time?      A. Yes.

Q. How long had you been there continuously in connection with the production of that film prior to the day that the [35] cameras turned?

A. About three weeks or better.

Q. This was at Goldwyn Studios, was it?

A. Yes, sir.

Q. By the way, does Goldwyn Studios make their studios available for lease or rental to so-called independent productions?

A. Not promiscuously.

Q. Do you know whether or not arrangements had been made for the use of their facilities for the picture "Copacabana"?      A. Yes, sir.

Q. By the way, during this three weeks' time which you were there, prior to the time the photography of this film started, can you tell us in a general short statement what you did? I do not want you to give us the details of the three weeks of

(Testimony of Maurice P. Koch.)

work, but in a general way what did you do during that period of time?

A. Well, I came down there on a call from Dave Hersh. They told me they were in a lot of trouble down there and they thought I had better come down. Perhaps I could possibly help them, straighten them out. I got down to Sam Goldwyn's studios. They had used up——

Q. Not what had happened, just what you did.

A. They were in trouble. They had used up all the preproduction money. The bank would not come forth with their money. They owed money to the help, to the musicians, to the [36] costume makers, and a strike was threatened at the studio that would have closed down Sam Coslow.

Q. Coslow or Goldwyn?

A. Sam Goldwyn Studios. The bank wouldn't put up their money. The bank reneged on some \$700,000.00, and since the Bank of America reneged, Standard Capital reneged along with them, and they had all the members of the corporation down there, sitting there with their hands on their heads and didn't know what to do, and I went in there. I called Max Fink on the phone, called him down there that night, and I told him to sue the Bank of America for a million dollars. We had a letter from the Bank of America stating that if we had all of the things that were necessary——

Q. May I stop you at this point, Mr. Koch.

A. Yes.

Q. I will show you here, Mr. Koch, a letter on

(Testimony of Maurice P. Koch.)

the letterhead of the Bank of America dated September 25, 1946, addressed to Mr. David Hersh. It purports to bear the signature of Bernard Giannini.

A. That is right. That was the letter—that was the basis upon which I was going to sue the Bank of America for a million dollars.

Mr. Fink: May I offer this letter in evidence, your Honor, as plaintiffs' next in order, and I should like to read it to the jury for the record, if I may. [37]

The Court: Any objection, counsel?

Mr. Gillard: No objection.

(The document referred to was thereupon marked Plaintiffs' Exhibit 11 and was read to the jury as follows:)

“Bank of America

“National Trust and Savings Association

“Los Angeles Main Office

“Los Angeles, California,

“September 25, 1946.

“Mr. David Hirsch,

“1041 North Formosa,

“Los Angeles 46, California.

“Re: Beacon Films, Inc.,

(Copa Cabana).

“Dear Mr. Hirsch:

“This Bank is prepared to enter into its usual form of Mortgage, Pledge and Assignment whereunder we are to lend the above-named corporation for the production of the pictured entitled “Copa

(Testimony of Maurice P. Koch.)

Cabana," to cost not in excess of \$1,100,000.00, the sum, whichever is less, of \$715,000.00 or sixty-five per cent of the negative cost of said picture with interest at the rate of five per cent per annum, based upon our understanding of the following pertinent facts:

"1. Said picture shall be produced at the Goldwyn Studios and will be released for distribution under an agreement with United Artists Corporation [38] satisfactory to the bank, and shall provide for a graudated distribution fee as follows:

Twenty-five per cent of the gross receipts until the negative cost is recovered or recouped; thereafter twenty-seven and one-half per cent of the gross receipts derived from domestic territory; thirty per cent from England; fifty per cent from South America; and thirty-seven and one-half per cent from Australia.

2. The producer shall be Sam Coslow and the director shall be Al Green. The cast shall feature and include Groucho Marx, Carmen Miranda, Steve Cochran, Gloria Jean and Andy Russell. The corporation shall engage the services of a controller or financial officer satisfactory to the bank and production supervision acceptable to the bank shall be provided.

3. The budget of the estimated production cost, the shooting schedule, the completion date, the borrowing period and the release date shall meet with the bank's approval.

4. Standard Capital will advance the sum of not



(Testimony of Maurice P. Koch.)

less than fifteen per cent of the negative cost toward the production and completion of the [39] picture, and will defer and subordinate its loans or advances to the bank's loans.

5. The remaining financing shall be made up of cash and deferments of compensation for services by the producer, director and principals of the cast.

6. Standard Capital will execute an unconditional Guaranty of Completion satisfactory to the bank, and will deposit as security for said guaranty an amount equal to at least fifteen per cent of the negative cost but not less than \$155,000.00.

“Yours Very Truly,

(s) “BERNARD GIANNINI,

(t) “BERNARD GIANNINI,

Vice President.”

Did you engage in any conferences with these financial institutions, that is, either Bank of America or Standard Capital during that three-weeks period?      A. I had you do that, Mr. Fink.

Q. Did you attend to the financial planning at the studio itself?      A. Yes.

Q. Was this bank loan made?

A. Yes, sir.

Q. Was the Standard Capital loan made?

A. Yes, sir. [40]

Q. Were the deferments of compensation obtained with regard to Groucho Marx and Carmen Miranda?      A. That is right.

Q. How much do they amount to, by the way?

(Testimony of Maurice P. Koch.)

A. Grouncho Marx was around \$100,000.00 or better, and I think Carmen Miranda was about \$50,000.00

Q. Mr. Koch, after you sent that first \$50,000.00, did you receive a note? A. Yes, sir.

Q. I show you here a note bearing date of August 31, 1946, and I will ask you if this is a photostat of a note that you received.

A. That is right.

Mr. Fink: May I offer this as plaintiffs' next in order, your Honor?

Mr. Gillard: No objection.

(Thereupon the document referred to was received in evidence and marked Plaintiffs' Exhibit 12.)

Q. (By Mr. Fink): After you advanced that first \$50,000.00 were there additional funds required for the preproduction of the picture "Copacabana"? A. Yes, sir.

Q. Did you advance some additional moneys?

A. Yes, sir.

Q. I will show you here what purports to be a check of [41] October 26, I believe, 1946, made payable to David Sebastian, signed by H. Koch & Sons by Rebecca Koch, that is, your sister, and partner you told us about, is that correct?

A. That is right.

Q. Is that her signature?

A. Yes, sir.

Q. The check is for \$30,000.00.

(Testimony of Maurice P. Koch.)

A. That is right.

Mr. Fink: I offer this as plaintiffs' exhibit next in order, your Honor.

(The document referred to was received in evidence and marked Plaintiff's Exhibit 13.)

Mr. Gillard: No objection.

Q. (By Mr. Fink): With regard to that \$30,000.00, did you receive a note?

A. Yes, sir.

Q. I show you here what purports to be a note of October 17, 1946, Beacon Pictures Corporation.

A. That is right.

Q. This is a photostat of the note that you received? A. That is right.

Mr. Fink: I offer this as plaintiffs' next in order, note of October 17, 1946, for \$30,000.00.

Mr. Gillard: No objection.

(The document referred to was thereupon received in evidence [42] and marked Plaintiffs' Exhibit 14.)

Q. (By Mr. Fink): Going back a bit, Mr. Koch, to the time that you gave your first \$50,000.00 check out, did you give that in response to the telegram requesting it? A. That is right.

Q. I will show you here a letter of August 12, 1946, which purports to have the signatures of David Hersh and Dave Sebastian on that letter.

A. Yes.

(Testimony of Maurice P. Koch.)

Mr. Fink: May I offer this as plaintiffs' next in order?

Mr. Gillard: No objection.

(The document referred to was thereupon received in evidence and marked Plaintiffs' Exhibit 15.)

Mr. Fink: May I read this to the jury, your Honor?

The Court: Very well.

(The document was read as follows:)

“Beacon Pictures Corporation

“August 12, 1946.

“Mr. Murray P. Koch,

“2224 Lake Street,

“San Francisco, California.

“Dear Murray:

“I am pleased to inform you that David Sebastian and myself have just concluded all negotiations necessary to complete our deal for the money from you to us to Beacon. We have arrived at a formula of 1.725 per unit of 10,000 [43] each, which will make a total of 8.625 for the \$50,000.00 which Dave brought back with him.

“The \$10,000 originally advanced to Dave Sebastian and subsequently turned over to me for capital investment in Beacon Pictures will be taken care of by the Hersh-Sebastian partnership interest in Beacon Pictures.

“The attorneys here are already drawing up the

(Testimony of Maurice P. Koch.)

collateral contract which should be ready in the next day or two. In the meantime, we think it advisable that we deposit the \$50,000.00 check in the account of Hersh-Sebastian for clearance, so that we can turn same over to Beacon Pictures as soon as the contract is ready. Unless you have objections to this arrangement, we will deposit this check in the Hersh-Sebastian account this next Wednesday, August 14, 1946. If there are any questions or doubts in your mind, wire us at this address to hold up the deposit.

“You will hear from us again later this week.

“Cordially,

“(s) DAVID HERSH,

“(t) DAVID HERSCH,

“(s) DAVE SEBASTIAN.”

Q. Calling your attention, Mr. Koch, to the month of August and of September, 1946, did you, during the course of that month, have discussions between yourself and Mr. Hersh, personal discussions, that is? [44]

A. Yes, sir, I had a lot of discussions with him when I was down there trying to get the money from the bank for the picture.

Mr. Gillard: I will move that the answer go out as not responsive to the question.

The Court: It may go out.

Q. (By Mr. Fink): Turning your attention to the time when you advanced the first \$50,000.00 and the time when you advanced the second, the \$30,000.00——

A. Yes.

(Testimony of Maurice P. Koch.)

Q. Did you during those times and in between those two times have personal discussions with Mr. Hersh?      A. Yes, I did.

Q. Did you also have telephone conversations with him?      A. A lot of them.

Q. Did you at the same times have personal discussions with Mr. Coslow?      A. Yes.

Q. And with Mr. Sebastian?

A. That is right.

Q. And telephone conversations also?

A. Yes, sir.

The Court: We will take a recess at this time for ten minutes. Remember the admonition heretofore given.

(Recess.) [45]

The Court: Proceed, counsel.

Q. (By Mr. Fink): I show you here a document entitled "Agreement," bearing date of August 31, 1946, between Murray P. Koch and Beacon Pictures, a corporation, and which bears two signatures, Murray P. Koch and Beacon Pictures Corporation by David Hersh, President. Do you recognize those signatures?      A. Yes, sir.

Q. Did you execute this document?

A. Right.

Q. Did you do so for yourself or on behalf of the partnership H. Koch & Sons?

A. On behalf of the partnership H. Koch & Sons.

(Testimony of Maurice P. Koch.)

Mr. Fink: May I offer this as plaintiffs' exhibit next in order, your Honor?

Mr. Gillard: No objection.

The Court: Exhibit 16.

(The document referred to was thereupon received in evidence and marked Plaintiffs' Exhibit 16.)

Q. (By Mr. Fink): Mr. Koch, at the time that you sent this additional \$30,000.00, or, rather, delivered another \$30,000.00 for the purpose of this picture, did you receive an amended agreement?

A. That is right, sir.

Q. I will show you here a document of October 17, 1946, which purports to bear your signature and that of George Frank, [46] Secretary.

A. That is right.

Q. Do you recognize those signatures?

A. Yes.

Mr. Fink: I will offer this as plaintiffs' next in order, your Honor.

The Court: Exhibit 17.

(The document referred to was thereupon received in evidence and marked Plaintiffs' Exhibit 17.)

Q. (By Mr. Fink): I show you here what purports to be a check of November 22, 1946.

A. Right.

Q. H. Koch & Sons, and underneath the signature of Maurice P. Koch. Is that your signature?

(Testimony of Maurice P. Koch.)

A. Yes.

Q. Check to Beacon Pictures Corporation.

A. That is right.

Mr. Fink: I offer this as plaintiffs' next in order, your Honor.

The Court: Exhibit 18.

(The check referred to was thereupon received in evidence and marked Plaintiffs' Exhibit 18.)

Mr. Fink: May I read this to the jury?

The Court: All right.

Mr. Fink: Exhibit 18 is a check on the form of Bank of [47] America, South Hollywood Branch, and that has been stricken out by pencil lines. Then "Hollywood" is stricken out and "San Francisco" is written in, and it says, "San Francisco, California, November 22, 1946. Pay to the order of Beacon Pictures Corporation \$20,000.00, H. Koch & Sons, Maurice P. Koch," and then the bank appears to be Pacific National Bank of San Francisco, 11-39. Then the blue stamp at the bottom "Endorsement missing."

Q. Mr. Koch, with regard to this check for \$20,000.00 where were you when you signed this?

A. Los Angeles.

Q. Where in Los Angeles?

A. I was at the bank—I was at the Bank of America. I believe it was the Hollywood Branch there some place.

Q. And you used one of their forms to make this



(Testimony of Maurice P. Koch.)

out on?           A. That is right, yes.

Q. Insofar as Beacon Pictures is concerned, did they return part of these picture funds that you had advanced in the year 1946?           A. No.

Q. Was that \$20,000.00 returned?

A. Oh, yes—well, that \$20,000.00—may I explain that?

Q. Yes, if you will, please.

A. When I was down there at the time that the bank wouldn't put up—the Bank of America wouldn't put up the seven hundred [48] and some odd thousand dollars, they were in a lot of other troubles there. They hadn't paid the musicians. They had started the production of the picture. They had not paid the musicians. They had not paid the dressmakers, and the union was going to picket the studios, and they needed money for salaries in order to prevent this, and there was quite a bit of turmoil. I came down there to straighten the whole thing out, and the only way to straighten it out was to put in another \$20,000.00, pay these people off, and get the studio open until the moneys came in from the Bank of America, and the agreement I made with the boys at the Beacon Pictures Corporation was that as soon as the money came in from the bank, after we had made—remade that loan, that I was to receive the \$20,000.00 back, and they agreed to do that. So we went down there and put up \$20,000.00 immediately and saved the studio from closing up.

Q. And this \$20,000.00 was returned?

(Testimony of Maurice P. Koch.)

A. Yes, sir.

Q. Was that after the bank loan, bank money and Standard Capital money was forthcoming?

A. That is right.

Q. After that money was available for the picture, you got back the \$20,000.00?

A. That is right.

Q. And this \$20,000.00 check, was that charged to the bank [49] account of H. Koch & Sons?

A. That is on the books, yes, sir.

Q. When that money was returned, that \$20,000.00, who did it go back to?

A. H. Koch & Sons, from where it came.

Q. Was there any practice with regard to the use of your name at times instead of the name H. Koch & Sons in business transactions?

A. A lot of times.

Q. I believe that check there bears date of October 22, 1946. When would you say it was that you got that \$20,000.00 back?

A. I believe that \$20,000.00 came back about a month after we loaned it to them, approximately.

Q. That would be practically the end of 1946?

A. I think so. I mean, the records will show when it came back.

Q. I think you told us that your original discussion with regard to setting up a venture to provide pre-production funds occurred early in the year 1946. During that year, up until the end of the year 1946, did you devote your time or part of your

(Testimony of Maurice P. Koch.)

time to that venture, including the things that you have told us about?

A. Yes, I spent a lot of time trying to promote some pictures, get them together, get the stories together, the stars together, get a deal together. [50]

Q. Turning to the beginning of the year 1947, that being the year in question here, was the picture "Copacabana" then in production? Was it then being filmed?

A. Yes, I believe it was completed the first part of the year.

Q. Prior to the completion of that picture did you come to know a man named Albert E. Green?

A. Yes.

Q. What business or occupation was he in?

A. Alfred Green was the director in "Copacabana." He made "The Jolson Story." He was the director of "Disraeli."

Q. "Disraeli"?

A. "Disraeli." He is quite a producer and a director, and I got to know him quite well while we were making the picture "Copacabana."

Q. From the beginning of the year 1947 did you have any discussions with Mr. Green with regard to independent picture ventures?

A. Yes, sir. As a matter of fact, I believe we drew up some kind of a paper on that whereby we would have Mr. Green's services——

Q. Not what was in the paper. That would not be proper for you to tell us at this time, Mr. Koch, but I show you here what purports to be a copy of

(Testimony of Maurice P. Koch.)

an unsigned document and ask you if you recognize this document.

A. Yes, yes, I know what this is. [51]

Q. By the way, you have told us, I believe, that you had counsel for your partnership H. Koch & Sons here in San Francisco, Mr. Grupp. Did you have counsel in Hollywood? A. Yes, sir.

Q. Who were your attorneys in Hollywood?

A. Fink, Levinthal & Kent.

Q. Was that document prepared to your knowledge? A. By Fink, yes, sir.

Q. Was it prepared at your instructions?

A. Yes, sir.

Q. I notice that the names mentioned as parties to this document are Maurice P. Koch——

Mr. Gillard: Just a minute, counsel. If your Honor please, I object to any testimony from the document until it has been offered in evidence and the Court has passed upon it.

The Court: I take it it is a preliminary question.

Mr. Fink: Yes, it is your Honor.

Q. Maurice P. Koch, Alfred E. Green, David A. Sebastian, and Sidney Rose. Prior to the drafting of this document before you, did you have conversations with the persons whose names we have just mentioned? A. Yes, sir.

Q. Where did these conversations occur?

A. Well, they occurred at your office. They occurred, I believe, at—— [52]

Q. By “your office”——

A. The office of Fink.

(Testimony of Maurice P. Koch.)

Q. Yes.

A. Fink's office. We had lunch together. We went over to Al Green's house. We talked this thing over quite a bit. We had quite a few meetings on this.

Q. Did you have meetings as a group, that is, the names mentioned there? A. Yes.

Q. Did you have individual discussions with the persons whose names you have mentioned?

A. Yes, sir.

Q. What was the subject matter of those discussions?

A. Well, we were discussing the life of Fred Fisher. We wanted to make a story on the life of Fred Fisher and one of the names of the features, Peg O' My Heart.

Q. That is the song title, Peg O' My Heart?

A. One of his song titles, yes, sir. We were going to have all the songs in the picture, though.

Mr. Fink: I offer this as plaintiffs' next in order.

Mr. Gillard: I object to it on the ground that no foundation has been laid.

The Court: I do not think there is yet, counsel, a foundation for that.

Mr. Fink: In that regard, your Honor, this document is not included. [53]

The Court: I realize that.

Mr. Fink: It is offered for the purpose of showing the activities of the plaintiffs in the motion pic-

(Testimony of Maurice P. Koch.)

ture insofar as promotion and financing of motion pictures are concerned in the year 1947.

The Court: But there isn't any foundation for it as yet, counsel, as I see it. You may ask the witness some further questions about it.

Q. (By Mr. Fink): Mr. Koch, was this document prepared at your direction?

A. Yes, sir.

Q. Was it prepared by counsel employed by the plaintiffs in this case? A. That is right.

Q. Did you see the document after it was prepared? A. I did.

Q. Subject to the deal of the Fred Fisher story, or whatever you want to call it, working out——

A. That is right.

Q. Was this document acceptable to you?

A. Yes, sir.

Q. Was it part of the effort you put forth in connection with the business of participating in a promotion and financing of motion pictures in the year 1947? A. That is right. [54]

Q. Was it prepared in the course of that business?

A. Yes, sir.

Mr. Fink: We offer it, your Honor, as plaintiff's next in order.

Mr. Gillard: It may be the Court should look at the document even as a matter such as Mr. Fink is talking about is concerned; this document has no relation at all to the question just asked of the witness.

Mr. Fink: If I may interrupt, your Honor——

The Court: Were you an officer or director of the corporation known as Amabssador Productions?

(Testimony of Maurice P. Koch.)

A. At one time I owned all the stock in Ambassador Productions.

Q. Did you own it at or about the time that this agreement was prepared?

A. No, sir. We were talking about——

Q. Just answer my question. A. No, sir.

Q. At the time this agreement was prepared, were you an officer or director of the corporation?

A. No, sir.

Q. Were you a stockholder in that corporation?

A. At the present time, no. I was subsequent to that agreement.

Q. The agreement provides, Mr. Koch, that you are the sole stockholder of the corporation.

A. I know, but that agreement was never executed and the [55] corporation—I never put any money in the corporation for that stock.

The Court: I do not think, counsel, that there has been any foundation yet laid.

Mr. Fink: But it will probably go along with other documents.

Q. Mr. Koch, was there a corporation called Ambassador Productions, Inc., organized?

Mr. Gillard: I object to that as not the best evidence.

The Court: It is preliminary. I will permit it.

The Witness: Ambassador Pictures, did you say?

Q. (By Mr. Fink): Ambassador Pictures or Ambassador Productions. Just one moment. Ambassador Productions, Inc. A. Yes, sir.

(Testimony of Maurice P. Koch.)

Q. At whose request was that corporation organized?      A. Organized at my request.

Q. Did you employ counsel for that purpose?

A. Yes, sir.

Q. Who were the counsel?      A. Fink.

Q. Why was that corporation organized? What was the purpose of it?

A. The purpose of that corporation was to set up a vehicle to make the picture which was the life of Fred Fisher. Subsequently it would have been called "Peg O' My Heart." [56]

Q. You told the Court, I believe, at the time this document wherein appears the names of Alfred Green, David Sebastian, Maurice P. Koch and Sidney Rose——      A. That is right.

Mr. Fink: May I have this marked for identification?

The Court: Let it be marked Exhibit 19 for identification.

(The document referred to was thereupon marked Plaintiffs' Exhibit 19 for identification.)

Q. (By Mr. Fink): At the time that Exhibit 19 was prepared by your counsel and under your direction, as you told us, had you intended to organize the company Ambassador Productions, Inc.?

A. That is right.

Q. Did you intend to cause stock to be issued of that organization?      A. That is right.

Q. Did you intend at that time to become the sole owner of all the shares of that corporation?



(Testimony of Maurice P. Koch.)

A. That is right.

Q. Had the shares been issued at the time this document was drafted?

A. No, no shares were issued at that time. I mean, there was no money to put up at that time.

Mr. Fink: I now offer in evidence, your Honor, the permit of the Department of Investment, State of California, the original, to Ambassador Productions, Inc., authorizing the [57] issuance of its shares of stock.

The Court: Do you contend that the shares were issued in accordance with the permit?

Mr. Fink: At a subsequent date, your Honor, yes.

The Court: They were issued?

Mr. Fink: Certain shares were issued at a subsequent date pursuant to this permit.

The Court: Exhibit 20.

(The permit referred to was thereupon received in evidence and marked Plaintiffs' Exhibit 20.)

Q. (By Mr. Fink): Prior to the issuance of shares and the completion of the corporate setup of Ambassador Productions, Inc., Mr. Koch, did you have other discussions? A. Yes.

Q. With the same people? A. Yes.

Q. Those mentioned in Exhibit 19?

A. Al Green.

Q. Yes.

A. Yes, we had a lot of discussions. As a matter of fact, we were going to sign a contract with Al

(Testimony of Maurice P. Koch.)

Green to make six pictures and he was going to direct those pictures.

Q. Prior to the time that any stock was issued in a corporation called Ambassador Productions, Inc., did you request that an agreement of employment between Alfred E. Green and [58] Ambassador Productions be prepared? A. That is right.

Q. I will show you here what purports to be a form of employment agreement by Ambassador Productions, Inc., by Alfred E. Green, which bears date of April 28, 1947, and it does not seem to have been executed. A. That is right.

Q. Was this the document to which you have reference? A. That is it.

Q. This document was prepared in 1947. We do not expect you to remember the contents of it. Will you tell us whether you were familiar with this document at the time it was prepared in the year 1947?

A. Well, yes, I was familiar with it because we did talk about a three-year contract and six feature-length pictures, which you have right here in the first paragraph.

Q. And were the discussions which you had preliminary to the carrying through of a deal to purchase a feature picture?

A. These were preliminary, yes.

Mr. Fink: We will offer the agreement between Ambassador Productions, Inc., and Alfred E. Green, dated April 28, 1947, your Honor, and again, if we may, renew our offer of Exhibit 19 for identification.

(Testimony of Maurice P. Koch.)

Since the permit for the issuance of the shares is now in the record, I believe the matters are now tied up perhaps more closely than they were previously.

Mr. Gillard: If the Court please, Exhibit 21, which refers to the employment contract between Ambassador Productions, or whatever that corporation is, and Al Green, is the activity of a corporation which this man is no part of. It is a corporate activity and not part of the activities of this individual, and as such has no relevancy to these proceedings as to whether he was in business.

The Court: That has not been marked but I will mark that, the employment contract, Exhibit 21 for identification. The objection to it may be sustained.

(The employment contract referred to was thereupon marked Plaintiffs' Exhibit 21 for identification.)

The Court: The witness has testified to certain transactions, but I as yet see no reason to admit the documents which were unexecuted by anybody. The former ruling stands as to Exhibit 19.

Q. (By Mr. Fink): For the moment, staying with this Ambassador Productions matter, Mr. Koch, eventually were there shares of stock in that corporation?

A. There was stock issued in that corporation. Shares, I guess.

Q. To whom were the shares issued?

A. I at one time owned all the shares in the corporation.

(Testimony of Maurice P. Koch.)

Q. Were the shares originally issued to you?

A. I can't remember if they were originally issued to me. [60]

Q. Did anybody else put any money in this company except you?      A. No, sir.

Q. Did anyone own any shares to your memory as long as you were active in that company?

A. No, sir.

Q. So far as your memory serves you, were you the only stockholder of that corporation?

A. Until I sold it, yes.

Q. You sold it in what year, Mr. Koch?

A. I think it was in 1948.

Q. That was after the year 1947, would you say, in this case?

A. Yes. It might have been—I doubt it. The record will speak for itself. I sold that to Jack Chertok, and I think there must be a record some place along the lines of the date that I sold it to him, if that is important.

Q. Going back for a moment to this picture "Copacabana", I will show you here a document entitled "Mortgage". It bears date of February 7, 1947. It purports to bear the signature of Beacon Pictures by David Hersh and Charles Weintraub, as President and Assistant Secretary, respectively. Do you recognize those signatures?      A. Yes, sir.

Q. It runs in favor of or to Murray P. Koch. By the way, do you sometimes use the name "Murray" instead of "Maurice"?

(Testimony of Maurice P. Koch.)

A. That happens to be my nickname, and I have had that ever [61] since I was in grammar school, and when I got in business about 30 years ago, they have used both of them, and I don't know whether I am coming or going.

Mr. Fink: We offer the mortgage of February 7, 1947, as plaintiffs' exhibit next in order.

Mr. Gillard: No objection.

The Court: It may be admitted as Exhibit 22.

(The mortgage referred to was thereupon received in evidence and marked Plaintiffs' Exhibit 22.)

Mr. Fink: May the record show with regard to all these documents that they have been exhibited first to counsel for the defendant, your Honor?

Mr. Gillard: That is correct.

Q. (By Mr. Fink): Mr. Koch, in connection with the Al Green deal—we will call it that for lack of a better name—was that transaction fully discussed between you and Mr. Green, Mr. Sebastian and Mr. Rose before the formation or before the activation of Ambassador Pictures? A. Yes, sir.

Q. Had you arrived at your exact thinking with these people prior to the activation of that corporation? A. That is right, we did.

Q. Was the document Exhibit 19 prepared at your direction prior to the activation of that corporation?

A. May I see that document? Yes. This was drawn up before [62] the corporation was formed. I believe it was. It must have been.

(Testimony of Maurice P. Koch.)

Mr. Fink: I offer in evidence a certified copy of the Articles of Incorporation of Ambassador Productions, Inc.

The Court: Exhibit 23.

(The document referred to was thereupon received in evidence and marked Plaintiffs' Exhibit 23.)

Mr. Fink: The filing stamp of the Secretary of State is March 20, 1947, your Honor.

Q. Mr. Koch, I show you here a copy of the Articles of Incorporation of Ambassador Productions, Inc., which seems to have been filed in the Secretary of State's office, Mr. Jordan's office, March 20, 1947, and I show you the incorporators of this corporation who signed these papers. The first name appears to be Cyrus Levinthal. Who is Cyrus Levinthal?

A. One of your partners.

Q. A lawyer? A. Lawyer, yes.

Q. In the office employed by you to set up this corporation? A. Yes.

Q. The name is Max Fink. A. Right.

Q. The same answer? A. Right.

Q. Leon E. Kent. [63] A. Yes.

Q. Raymond Hartmann. A. Right.

Q. Grace Gordon. A. That is right.

Q. Was she a lawyer?

A. No, she was the secretary.

Q. I see the acknowledgement is by Jerome D. Ralston. Who is he?

(Testimony of Maurice P. Koch.)

A. He is one of your partners and also a notary public.

Q. Do any of these people, the names that you have just called off, which appear to be all the incorporators, and all those persons whose names appear on these Articles of Incorporation appear to be in the law office of Fink, Ralston, Levinthal & Kent?

A. That is right.

Q. When you testified a moment ago I asked you certain questions in which I used the word "activation" of the corporation. Do you understand the difference between activating a corporation and merely organizing it or filing articles? A. No.

Q. Let me explain it this way. The filing of the articles for the purpose of my questions I will assume to be the mere skeleton organization. Activating it is when you put some meat on it, put some money into it. I will ask you, sir, at [64] the time these documents Exhibit 19 and Exhibit 21 were prepared, and at the time that you had these discussions with Mr. Green, Mr. Rose and Mr. Sebastian, that you told us about, had this corporation been set up to the extent of having any assets or liabilities?

A. No, it had not.

Q. You mentioned a few moments ago, Mr. Koch, that you had certain business dealings with a man named Chertok. A. Yes, sir.

Q. When did you first meet him?

A. I met Jack Chertok, it must have been the early part of 1947.

(Testimony of Maurice P. Koch.)

Q. What was the occasion for your getting together with him, meeting him?

A. I met him—I was interested in producing—not producing but promoting and financing some motion pictures, and he seemed to be quite a man in his business. He was with MGM for 25 years. He had made a lot of pictures. He had had a lot of Oscars and I got to like him very much. I liked his ability. I liked what he knew about the picture business.

Q. Did you have discussions with him with regard to motion picture projects?

A. Yes, sir. We got into quite a discussion on that and decided to make one big picture and a lot of little pictures.

Mr. Gillard: I am going to ask that the answer go out, if [65] the Court please. I move to strike it out. There is no foundation laid for the conversation.

The Court: The answer may go out.

Q. (By Mr. Fink): Mr. Koch, did you have the discussion with Mr. Chertok with regard to making a feature picture? A. Yes, sir.

Q. Where did that conversation occur?

A. That conversation occurred at the Friar's Club in Hollywood, California.

Q. Did you have more than one discussion with him upon that subject? A. Yes, sir.

Q. Did they occur in San Francisco, Los Angeles, or where?

A. No, we met at his house and another time we met him in San Francisco.

Q. In connection with this discussion in regard to



(Testimony of Maurice P. Koch.)

making a feature picture, was anything done about it?      A. Yes, sir.

Q. What was done?

A. Jack went back East. He was to find a good story. He found one book there called, "Hill of the Hawk."

Q. Was this a published book?

A. Yes, that book was written by Scott O'Dell.

Q. Did you at that time read the book?

A. Yes, sir. [66]

Q. Did members of your partnership other than yourself read that book?

A. Everybody read it, yes, sir.

Q. After reading the book, what was done?

A. We thought it was a pretty good story, and we thought we ought to make the picture, and we started proceedings—that is when we met down there with Jack Chertok. You were present when I gave you the first check for \$7,000.00 as a down payment for the rights to the story from Scott O'Dell.

Q. At the same time that you were active in connection with the Hill of the Hawk, did you discuss the making of other pictures?      A. Yes, sir.

Q. With those with Mr. Chertok?

A. We discussed a lot of B series pictures with Mr. Chertok, and that is what we discussed with Mr. Chertok at the time. Subsequent to the B pictures and The Hill of the Hawk, we went into the Government training pictures with Jack Chertok.

Q. All of this occurred in the year 1947, the year in question?

(Testimony of Maurice P. Koch.)

A. Yes, sir, we put a lot of money into that one. As a matter of fact, we promoted a million dollars for Jack Chertok on that training picture.

Mr. Fink: I offer in evidence as plaintiffs' exhibit next in order a letter from Annie Laurie Williams, October 17, 1946, addressed to Max Fink, re Hill of the Hawk by Scott O'Dell. [67] We have a stipulation from counsel that this letter was received by me or by my office shortly after the date which it bears.

Mr. Gillard: I will object to it, if the Court please, on the ground it is hearsay. It does not relate to the activities of this witness or his financial transactions.

Mr. Fink: Your Honor, this witness' activities are carried on by counsel, his agents, and by his lawyers.

The Court: Did you have any agreement with Mr. Chertok, written agreement?

The Witness: I had the stock of Ambassador Pictures Corporation—yes, I had notes.

The Court: Did you have any agreement with Mr. Chertok?

A. On Hill of the Hawk?

Q. Yes.

A. I might have. I don't remember. I might have some agreement with him.

Q. Did you make any agreement to produce any picture with Mr. Chertok?

A. Well, I made an agreement with him to finance and help promote money to make these pictures. They

(Testimony of Maurice P. Koch.)

were going to produce the pictures. I was going to finance money to promote the picture.

Q. What do you mean by that?

A. Well, when a picture is made you definitely have to have a [68] bank, money——

Q. You went through all that earlier today.

A. We have the same story here, Judge.

Q. What were you going to do in this matter?

A. Use it for pre-production. This particular money was for the payment—was—we were paying for the picture rights of the story by Scott O'Dell. That was *Hill of the Hawk*.

Q. Did you buy those rights?                      A. Yes, sir.

Q. Who?

A. Well, Ambassador Pictures bought them and I owned Ambassador Pictures. Is that correct, Mr. Fink?

The Court: Counsel, this seems to be a letter from somebody in New York which I, at the moment, cannot see the foundation for. I will mark it for identification.

Mr. Fink: May I be heard, your Honor?

The Court: That is 10/17/46. Exhibit 24 for identification.

(The document referred to was thereupon marked Plaintiffs' Exhibit 24 for identification.)

Q. (By Mr. Fink): Mr. Koch, at the time that you had your discussion and the negotiations that led up to the initial investigation into the purchase of the literary property called "*Hill of the Hawk*,"

(Testimony of Maurice P. Koch.)

was there any particular corporation mentioned? Did the corporation name of any kind enter into your [69] discussions? A. No, sir.

Q. You just told the Court that eventually Ambassador Productions took in its name the title to this literary property "Hill of the Hawk."

A. You mean before I put up money or after? I made the check out to Ambassador Pictures. I knew that Ambassador Pictures was going to buy Hill of the Hawk.

Q. When did you know that?

A. When we had lunch at the Frier's Club, and I gave you the check for \$7,000.00.

Q. Is that the first time you decided who was going to own that?

A. I knew we were going to use the corporation but I didn't know which one. I mean, I can't remember. That is 10 years ago. But I do know we made the checks out to Ambassador Pictures Corporation and you gave me all the stock of Ambassador Pictures Corporation as security for the money. That I do know.

Q. When did you say these discussions occurred between you and Mr. Chertok with regard to the making of a feature picture? I think you told us it preceded his trip to New York to find a story.

A. That is right.

Q. When did these first discussions occur?

A. These first discussions occurred the early part of 1947. [70]

Q. Were you advised whether or not Mr. Chertok made the trip to New York?

(Testimony of Maurice P. Koch.)

A. I knew he went to New York.

Mr. Gillard: I object to that as calling for the hearsay statement of the witness.

The Court: Overruled.

Q. (By Mr. Fink): Will you answer, please?

A. I knew he went to New York. I talked to him in New York.

Q. When was it, would you say, that you and your partners read the book "Hill of the Hawk" by Scott O'Dell?

A. That would be—that was sometime in 1947.

Q. By the way, what was the subject matter of this book? What was the nature of the story?

A. It was a beautiful story of early California days.

Q. At the time you first talked with Mr. Chertok about going to New York, at the time he went to New York, at the time you read the book "Hill of the Hawk"—during any of those times was Ambassador Productions or any other corporation name mentioned in your discussions?

A. Ambassador was mentioned. Yes. Yes, at the time we started to put money into Ambassador Productions, we knew we would need a lot of money for pre-production, and we possibly would not have enough of our own money, so we decided to form a corporation called Producers' Finance Corporation to finance money to promote and to produce pictures, to obtain money. [71]

Mr. Fink: I will offer in evidence, your Honor, as plaintiffs' next in order the Articles of Incorporation of Producers' Finance Corporation, which

(Testimony of Maurice P. Koch.)

bears date October 20, 1947, in accordance with the certification of the Secretary of State of California.

Mr. Gillard: No objection.

The Court: Exhibit 25.

(The document referred to was thereupon received in evidence and marked Plaintiffs' Exhibit 25.)

Q. (By Mr. Fink): Mr. Koch, turning to Exhibit 25, I will show you here the Articles of Incorporation of Producers Finance Corporation, and it appears to bear the names of three incorporators only.

A. Yes.

Q. Maurice P. Koch, San Francisco, California. That is you.

A. That is right.

Q. Morris M. Grupp, San Francisco, California. Who was that?

A. My San Francisco attorney.

Q. Was he acting at that time as the attorney for the partnership of H. Koch & Sons?

A. That is right.

Q. The third name and last name is Bernice E. Phillips. Who was that?

A. That was Mr. Grupp's secretary.

Q. Was this corporation, Producers' Finance Corporation, [72] organized by the attorney for H. Koch & Sons in San Francisco, Mr. Grupp and his office?

A. Yes, sir.

Q. Was he at that time acting for H. Koch & sons?

A. Yes, sir.

Q. Did you sign those papers acting on behalf of

(Testimony of Maurice P. Koch.)

the partnership?           A. That is right, sir.

Q. Will you tell us what was the purpose of that corporation?

A. That corporation was formed to obtain money from outside sources as well as our own to finance and promote pictures.

The Court: Is this a convenient place to take a recess?

Mr. Fink: Yes, your Honor.

The Court: We will take a recess at this time until 10:00 a.m. tomorrow morning. You will remember the admonition heretofore given you about not discussing the case, forming or expressing an opinion about it until it is finally submitted. 10:00 a.m. tomorrow morning. [73]

November 27, 1956—10:00 o'Clock A.M.

Mr. Gillard: If the Court please, may the defense have an order excluding witnesses from the courtroom? Yesterday I forgot to ask it.

The Court: It is a little late, counsel.

Mr. Gillard: I recognize that, your Honor.

The Court: Any objection to it?

Mr. Fink: The only two witnesses in the courtroom other than the witness on the witness stand are both from out of town and have nothing to do except to be in the courtroom.

The Court: All witnesses in the case of Koch vs. United States may retire from the courtroom. There is a witness room immediately across the hall.

## MAURICE P. KOCH

a plaintiff herein, being previously sworn, resumed the stand and testified further as follows:

## Direct Examination

(Resumed)

By Mr. Fink:

Q. Mr. Koch, calling your attention to on or about the month of September, approximately that time, in the year 1947, the year in question here, were there any negotiations with Monogram Pictures Corporation? A. Yes.

Q. What was that discussion about?

A. We negotiated with Monogram Pictures Corporation to produce [74] a lot of B pictures.

Q. What do you mean by a "B picture"?

A. A B picture would be cheaper picture than a big picture. The stars would be of lesser importance, the cost of the pictures would be smaller, and the expenses of making the picture would be a whole lot less than an A picture.

Q. Did you have counsel employed at that time for H. Koch & Sons with respect to the Monogram Pictures deal? A. Yes, sir.

Mr. Gillard: Counsel, may we have the "we" identified? He said "we" negotiated. May we find out who "we" was?

Q. (By Mr. Fink): Who was the "we" to whom you have reference?

A. Well, I negotiated for H. Koch & Sons and Mr. Fink was in my employ and was part of the negotiations.



(Testimony of Maurice P. Koch.)

Q. I will show you here what is called a production distribution agreement. Have you seen this document before?      A. Yes, sir.

Q. Do you recall approximately when it was that you first saw it?

A. I first saw this document while we were in Los Angeles there before the—this was somewhere around the time we were talking about Hill of the Hawk.

Mr. Fink: We have a stipulation, your Honor, that the letter of September 25, 1947, from Monogram Pictures Corporation was received by Max Fink. We offer the letter together with a [75] contract or document just identified as plaintiffs' next in order.

The Court: I do not understand what you are doing, counsel. Are you offering it in evidence?

Mr. Fink: Yes, your Honor.

The Court: That is what I did not hear.

Mr. Fink: We are offering the contract, together with the transmittal letter as one exhibit.

Mr. Gillard: I object to it as no foundation having been laid.

The Court: I am inclined to think that the objection is good, counsel.

Mr. Fink: I hesitate to call myself as a witness, your Honor, to identify a letter which obviously I received.

The Court: That is not the point of the objection, I do not believe. It was stipulated that you received the letter.

(Testimony of Maurice P. Koch.)

Mr. Fink: And the contract with it. I might note for the Court's attention the top of this letter has the technical staff of the Government's stamp on it, this same document having been in their possession for some years.

The Court: I take it that part is not questioned, that you received the letter and the contract. Whether it is admissible in evidence is the objection that is made.

Mr. Fink: We urge the admission of it upon the grounds that this voluminous contract for the production and distribution [76] of films shows the activity of the witness in the motion picture business.

The Court: I do not believe there is sufficient evidence to justify its admission yet, counsel. The objection may be sustained.

Mr. Fink: May we have it marked as plaintiffs' next in order?

The Court: 26 for identification.

(The document referred to was thereupon marked Plaintiffs' Exhibit 26 for identification.)

Mr. Fink: The letter and the contract are one exhibit, your Honor.

The Court: All right.

Q. (By Mr. Fink): Mr. Koch, are you familiar with the name Harry Fox or were you familiar with it in the year 1947? A. Yes.

Q. What was the nature of Harry Fox's activities in connection with the amusement business?

(Testimony of Maurice P. Koch.)

A. Harry Fox was one of the head people in the United States with relation to songs. He was situated in New York and he would find out for you or negotiate for you to find out if there were any plagiarisms on the songs or whether the songs were owned by the people that were supposed to have owned the songs, so that you would not run into too much difficulty if you would buy a series of songs or a play with the songs in them, [77] of having somebody sue you after you got involved in making the picture.

Q. Were there any negotiations conducted in your behalf—when I say “your behalf,” I have reference to H. Koch & Sons—many times I have asked things that you did, and I want you to know each time I have reference to H. Koch & Sons—did you or anyone in your behalf negotiate with Harry Fox for the acquisition of musical properties or songs for motion pictures?

Mr. Gillard: I object to that as incompetent, irrelevant and immaterial, whether anybody acted on his behalf.

Mr. Fink: A person may act through agents, attorneys and others employed by him with the same effect as if they acted for themselves.

The Court: That is true. It calls for a conculsion, counsel. If you have something to prove, get to the point and prove it. This is too general.

Q. (By Mr. Fink): I show you here, Mr. Koch, a letter of July 3, 1947, a letter of September 29, 1947, addressed purportedly by Harry Fox to Max Fink in each instance, and ask you if at the times of these

(Testimony of Maurice P. Koch.)

letters you know whether or not communications were being had with Harry Fox?      A. Yes, sir.

Q. Agent and trustee?      A. Yes, sir.

Q. Will you read these letters and tell me whether or not at [78] or about the date of those letters you were familiar with the general activity therein described?

A. Yes, this letter is from Harry Fox to Max Fink——

Q. That is all right. You can't tell us what is in the letter.

A. Oh, you asked me to read the letter.

Q. Read it to yourself. That is what I had in mind.

A. Yes, I am familiar with that letter. I am very familiar with that letter.

Mr. Fink: I will offer the letter of July 3, 1947, and the letter of September 29, 1947, to Harry Fox, your Honor, as plaintiffs' next in order.

Mr. Gillard: Objected to on the ground no foundation has been laid.

The Court: Counsel, there isn't any foundation as yet. The answer given by this witness is whether he is familiar with these letters, period. That is all you have shown. On that basis it is not admissible. A lot of people might be familiar with it for a lot of different reasons. I do not think there is any evidence yet that would justify the admission of these letters.

Mr. Fink: Do we, therefore, have in mind the objection having been made on the ground of lack of foundation; I was wondering if that goes only to the

(Testimony of Maurice P. Koch.)

problem of establishing the signature of Harry Fox? [79]

The Court: I do not know.

Mr. Fink: There would not be any other foundational problems that I know of. You will stipulate that I received the letters, will you not?

Mr. Gillard: I will stipulate that you received the letters, yes.

Mr. Fink: I am somewhat apprehensive about this objection, your Honor, because since I am apparently trying this law suit I do not want to become a witness. I can only tell your Honor——

The Court: That may be something that you do not desire to do, but this may become necessary for you. At the moment I can't see the basis for the admission of these letters in evidence. It may be you can establish it. I do not believe you have as yet. You might take your files, and he might have looked at your files and be familiar with them, and all your files would be admissible in evidence on that basis?

Mr. Fink: Your Honor, this has specific reference to the things he has testified to.

The Court: You have not developed from this witness anything that discloses that, counsel. I am not going to go any further with it.

Q. (By Mr. Fink): Mr. Koch, in order to clarify our record here, the letter of July 3, 1947, purports to be on the stationery of Harry Fox. It says, "In re: the story of Fred Fisher." [80]

A. That is right.

Q. On July 3, 1947, were you interested in a pro-

(Testimony of Maurice P. Koch.)

ject which I think you told us about yesterday called "The Story of Fred Fisher"?      A. Yes, sir.

Q. Were you interested at that time for the purpose of a motion picture venture in acquiring certain musical rights or song rights and live story rights with regard to Fred Fisher?      A. Yes, sir.

Q. At that time what was being done to acquire those rights, if anything?

Mr. Gillard: I object to that as vague and indefinite.

The Court: What did you do, Mr. Koch? Put the question that way?

A. I instructed Mr. Fink to get all the rights to the Fred Fisher story so that we could make a picture of it, and in doing this he had to go through the proper channels to see that everything was tied up properly so that no one could come back at us later and tell us that they owned a part of these songs or a part of this story, because it was an estate, and after you make a picture you could be sued for everything if someone else had an interest in it. And this is Mr. Fox's business of tying these things down.

A Juror: Your Honor, could the gentleman at the desk speak a little louder? I can never seem to get your remarks and I would like to hear what you say. [81]

Mr. Gillard: Thank you. I shall try to do that.

Mr. Fink: We offer this letter of July 3, 1947, on the letterhead of Harry Fox as plaintiffs' next in order.

Mr. Gillard: Same objection, and the further ob-

(Testimony of Maurice P. Koch.)

jection that there is no showing that Harry Fox was the agent employed or in any other fashion authorized to act on behalf of H. Koch & Sons.

The Court: I will admit the letter, there being no question about the fact that the letter was received by the person to whom it is addressed. Is that right?

Mr. Fink: Yes, your Honor.

The Court: Is that right, counsel?

Mr. Gillard: I have so stipulated, that is was received by Mr. Fink.

The Court: It may be marked Exhibit 27.

(The letter referred to was thereupon received in evidence and marked Plaintiffs' Exhibit 27.)

Q. (By Mr. Fink): Mr. Koch, I will show you a letter on what purports to be the stationary of Harry Fox, agent and trustee, dated September 29, 1947, which purports to also relate to the Fred Fisher matter. A. That is right.

Q. On or about the date of September 29, 1947, was Max Fink still acting as your attorney?

A. Yes, sir. [82]

Q. Was he acting in connection with the matter of clearing title to Fred Fisher's songs and story?

A. That is right, sir.

Mr. Fink: May I offer this as plaintiffs' exhibit next in order, your Honor?

Mr. Gillard: Same objection.

The Court: What is it?

Mr. Gillard: No foundation has been laid, and that there is no indication that Harry Fox was an

(Testimony of Maurice P. Koch.)

agent employed or otherwise authorized to act for or on behalf of H. Koch & Sons.

Mr. Fink: It is not contended that Harry Fox was acting for H. Koch & Sons. He was acting for the Fishers, if for anyone. The letters are offered to show the activities that went on, your Honor.

The Court: Is it stipulated that the letter was received by Max Fink? You say there is no foundation. I don't know what you mean by no foundation, counsel. Do you mean it is not signed by Fox, was not received by Fink?

Mr. Gillard: That is correct, your Honor. All I have stipulated to is that the letter was received by Mr. Max Fink. I have not stipulated it was signed by Harry Fox, on his behalf, or by anybody authorized to do so on behalf of H. Koch & Sons.

The Court: It may be admitted as Exhibit 28.

(The document referred to was thereupon received in evidence and marked Plaintiffs Exhibit 28.) [83]

Q. (By Mr. Fink): Mr. Koch, we exhibited to you a while ago a matter relating to Monogram Pictures, Exhibit 26, I believe, for identification at this time. I called your attention to September 25, 1947, at that time. And now I will ask you if on or about November 19, 1947, your negotiations with Monogram Pictures Corporation were still in progress?

A. We were in a lot of other activities then, and they were still writing us, trying to get us——

Q. Not what they were writing you; I do not be-



(Testimony of Maurice P. Koch.)

lieve that you would have the right to tell us the contents of any document, Mr. Koch. Just tell us what was happening. Were there revisions being made to contracts?      A. Yes.

Q. And negotiations were being conducted over a period of months?      A. That is right.

Q. I will show you here a letter of November 19, 1947, and I will ask you if you will read that letter to yourself, please.

A. Yes, I have seen that letter.

Q. On the date that this letter bears, November 19, 1947, were these negotiations and revisions still going on with Monogram Pictures Corporation?

A. They were.

Mr. Fink: I will offer the letter of November 19, 1947, your Honor, as plaintiffs' next in order. [84]

Mr. Gillard: I will object on the ground that there is no foundation laid, if the Court please. There is no showing that Mr. Fink was acting on behalf of the witness in this connection. The evidence shows that Mr. Fink was a director of Ambassador Pictures Corporation. There is nothing to indicate that he was not acting in that capacity rather than in a capacity for H. Koch & Sons, as distinguished from any corporate activity that H. Koch & Sons was interested in.

Mr. Fink: May I be heard, your Honor?

The Court: Yes.

Mr. Fink: It is rather difficult at best to cover situations that occurred 10 years ago. I have the feeling that the introduction of these documents and

(Testimony of Maurice P. Koch.)

letters would help us revive and reconstruct this situation for the Court and the Jury, and I do believe, although each letter in and of itself may not be important, it helps to tell the story as is occurred 10 years ago.

The Court: However, I believe the objection made by the Government is good. It has not been met by the plaintiffs.

Mr. Fink: May we have it marked?

The Court: It may be marked.

Mr. Fink: We have a stipulation with regard to this letter that is was received, do we not, counsel?

Mr. Gillard: Yes.

The Court: Exhibit 29 for identification. [85]

(The document referred to was thereupon marked Plaintiffs' Exhibit 29 for identification.)

Mr. Fink: We do have a stipulation that the letter was received by our office, counsel?

Mr. Gillard: That is correct.

Mr. Fink: Thank you.

Q. In connection with acquiring the motion picture rights to the book "Hill of the Hawk" by Scott O'Dell, did you have business with Annie Laurie Williams of New York City?

A. Through you, yes.

Q. When you say "you", you have reference to Max Fink? A. That is right.

Q. Or Fink, Ralston, Levinthal and Kent?

A. That is right.

Q. What instructions did you give to your coun-

(Testimony of Maurice P. Koch.)

sel in connection with Hill of the Hawk, the purchase or acquisition of the Hill of the Hawk story and book for picture purposes?

A. I asked you to buy the picture rights of the book. I asked you to protect us against all things that might lead to legal entanglements later on when we would get into the picture, and act as my legal counsel in the matter, protect my interests.

Q. In the months of October, November and December of 1947, and all during the year 1948, did the same attorneys continue to act for you in connection with the Hill of the Hawk story?

A. Yes, sir. [86]

Q. I will ask you to look at these papers that I placed before you and tell us whether or not on the dates mentioned on these documents to your knowledge efforts were being made for the purpose of acquiring Hill of the Hawk?

A. That is right.

Mr. Gillard: I object to that as calling for the opinion and conclusion of the witness.

The Court: Sustained.

Mr. Fink: I offer at this time, your Honor, copy of letter of Max Fink addressed to Annie Laurie Williams, New York. It may be a little cumbersome for our record, your Honor, but I would prefer to offer these one by one if I may. We offer first the letter of October 24, 1947.

Mr. Gillard: I object to it as no foundation having been laid.

Mr. Fink: May we have a stipulation that the

(Testimony of Maurice P. Koch.)

original was sent in accordance with the ordinary course of business?

Mr. Gillard: No.

The Court: Counsel, this witness can testify as to what he did and to what instructions he gave, what activities he had, but I do not believe through this witness you can produce evidence of what somebody else did because he doesn't know anything about it. You can ask him as to what he did, what instructions he gave, what activities he engaged in in connection with such matters as may be relevant, but I think if you [87] intend to prove the activities of some other people, you have to produce some other witnesses.

Mr. Fink: I rather expected certain stipulations, your Honor, on these routine matters. Since we do not have them——

Mr. Gillard: I am going to move that that be stricken, if the Court please.

The Court: It may go out. The statement of counsel is not evidence. It may be stricken.

Q. (By Mr. Fink): Mr. Koch, I show you here a document which bears date of December 12, 1947, entitled "Agreement" between Ambassador Pictures, Inc., as the purchaser, and Scott O'Dell as the owner, or called the owner in this agreement.

A. Yes, sir.

Q. Are you familiar with this document?

A. Yes, sir.

Q. I show you here the signature on the last

(Testimony of Maurice P. Koch.)

page of this document, Exhibit A-5, of Jack Chertok. Are you familiar with his signature?

A. Yes, sir.

Q. Is that his signature?                      A. It is.

Q. I will show you here the signature on page 13 of the document which precedes the exhibit we refer to and ask you if you recognize the signature that purports to be that of Jack Chertok?

A. That is right. [88]

Mr. Fink: I will offer this document as plaintiffs' next in order, your Honor, and I should like to note for the record that in the upper left-hand corner it bears the stamp of the technical staff. This document was in their possession. That is to be disregarded, I assume, for the purpose of this trial.

Mr. Gillard: I object on the ground it is incompetent, irrelevant and immaterial, and not bearing upon the issues of this case.

The Court: Counsel, I can't see the basis at the present time for the admission of this.

Mr. Fink: I was wondering, your Honor, if it would be helpful for us to discuss the law of the case in relation to these matters.

The Court: Do you desire a recess for that purpose?

Mr. Fink: I think it would be helpful.

The Court: We will take a recess.

(Recess.)

Q. (By Mr. Fink): Mr. Koch, going back for a moment to this Monogram Pictures Corporation,

(Testimony of Maurice P. Koch.)

the matter that we were discussing a while ago with reference to the so-called Class B pictures you told us about, over what period of time were those negotiations carried on?

A. Those negotiations were carried on during the first part of 1947. It might have been the end of 1946. They were carried on for months. [89]

Q. What was your participation, what activity or what part did you play on behalf of H. Koch & Sons in connection with these matters? What did you do?

A. I was down in Los Angeles for conferences. I participated in the deals. There were a lot of changes made in how we were going into the deal and how we were going to make the pictures and what kind of budgets we were going to use and how much money a picture would cost, because we were going to make a series of pictures, and how much money the Monogram people were going to put up in the pre-production with us. I was active in the entire transaction at all times.

Q. During all of this time were you acting for H. Koch & Sons?      A. Yes, sir.

Q. That is for your brothers and your sister?

A. That is right.

Q. Were your expenses being paid?

A. By H. Koch & Sons, yes, sir.

Q. By the partnership?      A. Yes, sir.

Q. Was that true, by the way, throughout all these motion picture transactions?

A. That is right, sir.

(Testimony of Maurice P. Koch.)

June 9, 1948, which purports to be drawn on the Trust Account of Fink, Ralston, Levinthal & Kent to Annie Laurie Williams, Inc., for \$5,000.00.

A. Yes, sir.

Q. Do you recognize the signature of Cyrus Levinthal?      A. Yes, sir.

Q. You have known Cyrus Levinthal for how long now?

A. I have known Mr. Levinthal for over 25 years.

Mr. Fink: We will offer these two checks as one exhibit, plaintiffs' next in order.

Mr. Gillard: To the check dated June 8, 1948, payable to Max Fink, for \$5,000.00 drawn by Maurice P. Koch, I will object to it on the ground there is no showing that that check has any connection with this case whatsoever. It is merely a check from Maurice Koch to Max Fink. The second check from Fink, Ralson, Levinthal & Kent, I will object to on the ground no foundation has been laid in any way, shape or form, to introduce that check in [95] evidence.

The Court: There is no testimony as to what the purpose of these checks was, as yet.

Q. (By Mr. Fink): Mr. Koch, the check of June 8, 1948, to Max Fink, for \$5,000, what was that for?

A. That was the second payment for the rights to the picture, "Hill of the Hawk."

Q. Did you give your attorneys any instructions as to what to do with that money?

(Testimony of Maurice P. Koch.)

A. Yes, sir.

Q. What were the instructions?

A. The instructions were to send the \$5,000 to Scott Odell or his agents.

Q. Who were his agents?

A. Annie Laurie Williams.

Mr. Fink: We offer the two checks, your Honor.

The Court: The checks are dated in 1948.

The Witness: Yes, sir.

The Court: They may be admitted and marked Exhibit 32.

(The two checks referred to were marked Plaintiffs' Exhibit No 32 in evidence.)

Q. (By Mr. Fink): Mr. Koch, on or about May 9th or May 10th, 1948, did you give some money to Fink, Ralston, Levinthal & Kent?

A. I might have.

Q. How much? [96]

A. Well——

Mr. Gillard: I object to that as no foundation having been laid. He doesn't even know if he gave any.

Q. (By Mr. Fink): Let me ask this question: What was the total cash amount paid for "Hill of the Hawk"? A. \$25,000.

Q. With the exception of the first \$7,000 that you told us which went to purchase stock of Ambassador Pictures—— A. Yes, sir.



(Testimony of Maurice P. Koch.)

Q. —has that \$7,000, after Ambassador Pictures got it, what was done with it?

A. It was sent to Annie Laurie Williams for the purchase of the rights of "Hill of the Hawk."

Q. That left \$18,000 unpaid, according to my arithmetic.

A. That is right.

Q. And that \$18,000, how was it paid?

A. The first payment was \$7,000. The next payment was \$5,000, and which I gave you a check for. The next payment was another \$5,000, which I gave you a check for. The last payment was \$8,000, which you also received a check for.

Q. I will show you here two checks of May 10th, one for \$4,500 and one for \$500, to be drawn on the Fink, Ralston, Levinthal & Kent trust account by Jerry Ralston. Do you recognize the signature of Jerry Ralston?

A. Yes, sir. [97]

Mr. Fink: We offer these two checks, your Honor, as plaintiffs' next in order.

Mr. Gillard: I object to them as being the activities of a third person not related to this case.

The Court: I take it one thing we should get clear to the jury is that the important thing we are interested in are the activities of this witness and of H. Koch and Sons for the year 1947. Is that correct?

Mr. Fink: Yes, your Honor.

The Court: These checks may be admitted as a part of a transaction which commenced in 1947, to show, if they do show, what the activities were in 1947.

(Testimony of Maurice P. Koch.)

Mr. Fink: Yes, your Honor. Our position, of course, is that the acts of their lawyers are just like their own acts.

The Court: Yes, but that is not the point. This is done in 1948.

Mr. Fink: As your Honor has pointed out, something started in 1947.

The Court: All right, it may be admitted for that purpose, Exhibit 33.

(The two checks referred to were marked Plaintiffs' Exhibit No. 33 in evidence.)

Q. (By Mr. Fink): I will show you check of July 9, 1948, made payable to Annie Laurie Williams, Inc., signed "Fink, Ralston, Levinthal & Kent, Trust Account, by Max Fink." Do [98] you recognize the signature of Max Fink?

A. Yes, sir.

Mr. Fink: Your Honor, these checks may be put together as one exhibit.

The Court: I think they should be part of Exhibit 33, which we just admitted in evidence.

Mr. Fink: Yes.

The Court: And it is admitted for the same purpose, to show, if it does show, any activities in the year 1947.

Gentlemen, we are going to take a recess at this time until two o'clock, and as I have told counsel in chambers, many of these things that are now being presented should have been taken care of in a pre-trial procedure so that the time of the jury and

(Testimony of Maurice P. Koch.)

Q. Returning now to "Hill of the Hawk," I believe you told us that you, that Ambassador Pictures acquired a book called "Hill of the Hawk," the motion picture rights to that book? [90]

A. That is right.

Q. Were there negotiations to your knowledge with regard to the acquisition of that property?

Mr. Gillard: I object to that as incompetent, irrelevant and immaterial.

The Court: I take it that is preliminary. It may be answered.

(To the witness.) Yes or no.

The Witness: Yes.

Q. (By Mr. Fink): What did you do in that connection?

A. I went down to Los Angeles. I discussed the property with you and gave you instructions to purchase the story of "Hill of the Hawk" for Ambassador Pictures Corporation, and for the production corporation. The negotiations of this, and the type of contract that we got, that we received from Scott O'Dell was very important. I sat in on these negotiations with you before the transactions were completed.

Q. Where did Mr. O'Dell live?

A. Mr. O'Dell lived back East.

Q. Did you ever meet Scott O'Dell?

A. I believe I met Scott O'Dell at Jack Chertok's house in your presence.

Q. Did you talk with him about the story of "Hill of the Hawk"? A. Yes, sir.

(Testimony of Maurice P. Koch.)

“Q. Did you spend any time discussing point of view with regard [91] to how a picture was to be made from that story? A. Yes, sir.

Q. To what extent?

A. We talked to the extent that we knew that it had to be a top cast. It had to have women in there, particularly one woman, with a lot of fire, possibly a little Latin in her. We needed characters such as Akim Tamiroff for a father, possibly a person like Gary Cooper for lead in the picture, Jennifer Jones—we figured on Jennifer Jones for the fiery woman, because she’s got a little Indian in her.

Q. I show you here a check of December 3, 1947. It purports to bear your signature.

A. Yes, sir.

Q. Is that your signature? A. Yes, sir.

Q. You noticed the date of December 3, 1947?

A. That is right.

Q. The check was made to Ambassador Pictures Corporation, is that right? A. That is right.

Mr. Fink: We will ask that this be marked plaintiff’s next in order, Your Honor.

The Court: Exhibit 30.

(The check referred to was thereupon received in evidence and marked Plaintiffs’ Exhibit 30.) [92]

Mr. Fink: May we indicate the check is for \$7,000.00?

Q. Do you recall where you were at the time you made out that check?

(Testimony of Maurice P. Koch.)

A. Yes, sir, I was at the Friar's Club in Hollywood.

Q. Who was present?

A. Milton Crasney, Dave Sebastian, Max Fink and myself.

Q. And Jack Chertok?

A. And Jack Chertok, yes, sir.

Q. What is Milton Crasney's business?

A. Milton Crasney is an agent and producer. He sells a lot of television shows on a percentage basis and he is doing quite a business at the present time.

Q. Do you know whether or not he is connected with a company called Gene Artists Corpoation?

A. That is right.

Q. Called G.A.C. in the industry?

A. That is right.

Mr. Fink: May we at this time offer as plaintiffs' next in order, Your Honor, the agreement between Scott O'Dell and Ambassador Pictures of December 12, 1947?

The Court: Is it an executed document?

Mr. Fink: Yes, Your Honor. The witness has identified at least the signature of the purchasing party.

Mr. Gillard: I object to that as incompetent, irrelevant and immaterial, not bearing upon the issues of this case. The [93] activity of the Ambassador Pictures Corporation is not the activity of this witness.

(Testimony of Maurice P. Koch.)

The Court: It may be received solely for the purpose of showing that a contract was entered into as of the date that it bears. All of the detail that is in the contract, I take it, is not pertinent to this inquiry. It may be introduced for the purpose of showing that there was a contract that was entered into as of the date it bears.

(The agreement referred to was thereupon received in evidence and marked Plaintiffs' Exhibit 31.)

Q. (By Mr. Fink): Now, what was the purpose of making out that \$7,000.00 check just referred to, Mr. Koch?

A. The purpose of making out that check was to buy the stock of Ambassador Pictures Corporation.

Q. Did you know what the \$7,000.00 was going to be used for?      A. Yes, sir.

Q. What was that?

A. The purchase of "Hill of the Hawk."

Q. Was that the full purchase price or the down payment?

A. That was the first down payment, \$25,000.00.

Q. Mr. Koch, I show you here a check of June 8, 1948, to Max Fink for \$5,000.00 and ask you if that is your signature, Maurice Koch?

A. Yes, sir.

Q. Did you pay out that \$5,000.00 to Max [94] Fink?      A. Yes, sir.

Q. I show you a check of the following day,

(Testimony of Maurice P. Koch.)

the Court should not be taken up. By the time you come back at two o'clock I expect you to show all documents to the other side that you are going to offer, so that they have an opportunity to examine them, and that we shall not waste the time of the Court and the jury sitting here while counsel is looking at documents.

How many more documents do you have?

Mr. Fink: They have all been before counsel. I have put them there so counsel can see them all, yesterday and today.

The Court: Why do we wait such a long time for the reading of them?

Mr. Gillard: If your Honor please, I got handed yesterday [99] morning during the course of the trial a stack of about 75 documents. You can recognize during that period of time I did not have a chance to look at them carefully because there was no opportunity while the case was going on.

Mr. Fink: I think the Government has always had copies of the important papers, the longer papers.

Mr. Gillard: I do not think we should encumber the record unnecessarily with this discussion. They gave me seven copies of documents.

The Court: Gentlemen, all of these things should have been done, as I stated before, in a pre-trial procedure, before you ever came into court. I am going to give you until two o'clock to examine all the documents, so that when we go ahead at two o'clock this afternoon we are not going to be faced

(Testimony of Maurice P. Koch.)

by delays by a document being presented then, and the Court and jury sitting here while it is being examined.

We will take a recess at this time until 2:00 o'clock.

(Whereupon a recess was taken until 2:00 p.m.) [100]

Tuesday, November 27, 1956, 2:00 P.M.

The Court: Proceed.

Mr. Fink: By stipulation, your Honor, I should like to offer as one exhibit letter from H. Koch and Sons, signed "Murray," July 8, 1948; copy of reply to that letter signed July 9, 1948.

The Court: It may be introduced and marked Exhibit 34.

(The two letters referred to was marked Plaintiffs' Exhibit No. 34 in evidence.)

Mr. Fink: May I read these into the record and to the jury, your Honor?

The Court: All right.

Mr. Fink: Letter dated July 8, 1948, Exhibit 34, on the letterhead of H. Koch & Sons, Luggage Manufacturers, 73 Beale Street, San Francisco 5, California:

"Dear Max:

"Enclosed you will find the last payment which is \$8,000, for the book 'Hill of the Hawk.' It is not



(Testimony of Maurice P. Koch.)

necessary for me to tell you to be sure that this book is tied up completely, as \$25,000 isn't 'hay.'

"Will you please send me some sort of a letter advising me that the book is completely paid for and the property of Ambassador Pictures Corp., of which [101] I own all of the stock now, for after all I am responsible to the stockholders and I do not even have a piece of paper showing ownership of this book, as you know all of that is in your office where it should be kept. I should have some evidence of that fact in my files in San Francisco for my stockholders' benefit.

"Please let me hear from you on the above as soon as possible.

"With kindest regards, I am,

"Sincerely,

"MURRAY."

And it shows "Enclosure: Check."

The response to that is dated July 9, 1948, the next day, addressed to Mr. Murray Koch, care of H. Koch & Sons, 73 Beale Street, San Francisco 5, California:

"Dear Murray:

"This will acknowledge receipt from you of your check in the sum of \$8,000, which we this day deposited in our trust account. We have this day forwarded our trust account check to Annie Laurie Williams, Inc., agents for Scott O'Dell, author, in the sum of \$8,000, which constitutes our final pay-

(Testimony of Maurice P. Koch.)

ment in the acquisition of "Hill of the Hawk" by Ambassador Pictures, Inc.

"You have paid the sum of \$25,000, which constitutes [102] the entire cash price to be paid for the motion picture rights on 'Hill of the Hawk.' In addition to the sum of \$25,000, Mr. O'Dell is entitled to 5% of the 'net profits,' as the said term is defined in the purchase agreement.

"The ownership of the motion picture rights of 'Hill of the Hawk' is held by Ambassador Pictures, Inc., and all of the outstanding stock of the said corporation has been issued to you and now remains in your name. Under the circumstances, the corporation is entirely under your control.

"Kindest personal regards,

"Yours sincerely,

"MAX FINK."

Q. Mr. Koch, in your letter of July 8, 1948, addressed to Mr. Max Fink, you used the words as follows: "for after all I am responsible to the stockholders \* \* \*" Whom did you have in mind when you wrote the word "stockholders" in this letter?

A. My partners.

Q. During the balance of the year, 1948—I won't go beyond that—did you continue to be the sole stockholder, or did all the stock of that corporation stand in your name?      A. Yes, sir.

Q. I believe you told us yesterday that you became involved [103] in some films made for the Signal Corps, and also for the Air Corps.

(Testimony of Maurice P. Koch.)

A. Yes, sir.

Q. When I say "you," I have reference to H. Koch & Sons. Do you understand that?

A. That is right.

Q. Approximately when did the project of making training films first start? I mean the discussions that led up to it?

A. The discussions that led up to the training films first started in 1947.

Q. About when, in that year?

A. I can't tell you exactly when, but it was the latter part of 1947.

Q. In any event, in the year 1947, what was done with regard to the project of these films?

A. The project was discussed, and preproduction money was needed before we could put in a bid for the contract.

Q. Was the financing generally for the making of these films required prior to contracting for them?

A. Yes, sir, because if the preproduction money was not there, and they were awarded the contract, they could not get started.

Q. Were you called upon to make any proofs of the availability of all the money necessary to produce such films?

A. Mr. Chertok took our word for it. We convinced them that [104] we were capable of providing the money, and that was satisfactory with Mr. Chertok.

Q. What did you do in the year 1947 prelim-

(Testimony of Maurice P. Koch.)

inary to the actual contracting for these films and the production of them?

A. Well, we had Mr. Miller up here, and Mr. Chertok. I introduced them to the president of our bank.

Q. Which bank is that?

A. Pacific National Bank.

Q. In San Francisco?

A. In San Francisco. Before they came up here I went down to see Mr. Lee Masters, who is the president of the Pacific National Bank, and told him that I had a terrific deal for him whereby the money would be fairly safe and it would be a good business deal for him, whereby we needed over a million dollars to finance 30 or 40 training pictures for the government, important pictures, and I told him that I was interested in the transaction; that we would supply all of the preproduction money for these training films, and that they would get their money back after completion, or the negative of the film. And I told Mr. Lee Masters that these films were going to be produced by Apex Film Corporation on Vine Street in Hollywood—Lysenko, rather, in Hollywood. I believe that is where his offices were at the time. And I gave them quite a history of Jack Chertok. I told him that [105] Jack was with M.G.M. for over 25 years; he had a lot of "Oscars"; he was a great producer; he had produced a lot of pictures. He had produced "Lone Ranger" pictures for television for General Mills, and was one of the most

(Testimony of Maurice P. Koch.)

competent men and most thought of men in Hollywood, and that I would recommend him very highly.

Q. Prior to the time that you had this discussion with the bankers how many times had you visited with Mr. Chertok with regard to the project of making training films?

A. I visited with him several times. We had a lot of discussions on these training films. We wanted to see the paper work on it. We wanted to know where the money was coming from, from the government; how secure the transaction would be; and the capabilities of Apex Film Corporation in making these films.

Q. How much time would you say you spent in Los Angeles in the year 1947 in preparation for this project?

A. We had many conferences together. I would say I spent a lot of time. I can't remember how much time, but I spent an awful lot of time with him.

Q. By the way, we mentioned this morning a company called Producers Finance Corporation, which I believe you told us was incorporated at your request by Mr. Grupp, an attorney here in San Francisco.

A. Right. [106]

Q. Did Mr. Grupp ever attend with you in Los Angeles during the year 1947 in connection with these training films?

A. Yes, sir, Mr. Grupp went down there.

Q. Were you with him? A. Yes, sir.

Q. What happened? What did you do there?

(Testimony of Maurice P. Koch.)

A. We discussed the financing of these various training films.

Q. Subsequent to all of these discussions, I show you here what purports to be copies of telegrams, one bearing date of January 14, 1948, and one January 15, 1948; a notice of award bearing date of January 14, 1948. I will ask you if you received copies of these documents?           A. Yes, sir.

Q. Did you receive these copies, or these documents, in connection with your activities in the financing of this project?

A. Yes, sir. I had to know what was going on on this project all the time. I had to be kept informed because I was involved——

Q. The question is, were you informed?

A. Yes, sir.

Q. Did you keep yourself informed?

A. Yes, sir.

Q. Did you continue to be active on this [107] project?

A. Until the completion of the project, yes, sir.

Q. Did you, first of all, loan some moneys?

A. Yes, sir, we did loan some moneys to Apex Film Corporation.

Q. I show you a check of January 27, 1948. It seems to be drawn January 26, 1948.

Mr. Gillard: Pardon me, Counsel. Before you describe the check would you mind making an offer and allowing an objection to be made to it?

Mr. Fink: Do you object to the foundation, Counsel?

(Testimony of Maurice P. Koch.)

Mr. Gillard: Certainly.

Q. (By Mr. Fink): Mr. Koch, is this your signature? A. Yes, sir.

Mr. Fink: May I offer this check, your Honor, as plaintiffs' next in order?

Mr. Gillard: If the Court please, the evidence so far with reference to this Producers Finance Corporation and the manual training films that the witness has just testified to, the testimony indicates that there were preliminary discussions in 1947 which had not jelled into anything. It now appears that the first financial transaction that this witness was in was in 1948, which is subsequent to the year in issue in this suit, and on that ground I will object to any evidence of the financial arrangements with reference to Producers Finance Corporation or Apex Films in 1948. [108]

Mr. Fink: Our position, your Honor, if I may state it, is that this project was conceived and the financing was committed in the year 1947, or there could not have been any proposals or bids made to the company which gave rise to the final contracts which occurred in January of the following year, and that naturally, until you get a contract from the government, there was no need in spending any money. It is true that this check bears date of January 26, 1948.

The Court: I think the witness can testify to his activities in connection with this matter in 1947, and may generally say that payments were made in 1948, if that were the fact. But as to the details of

(Testimony of Maurice P. Koch.)

the individual checks, I do not believe they would be admissible if they were delivered in 1948, and the only reason for showing activity in 1948 is to show, if it does show, what the activities were in 1947.

Q. (By Mr. Fink): Mr. Koch, pursuant to these discussions and negotiations you told us about in 1947, did you thereafter make available funds, your funds, funds of H. Koch & Sons, and funds of Producers Finance Corporation, for this project?

A. Yes, sir.

Q. Did you arrange the million-dollar loan you were talking about a moment ago?

A. Yes, sir.

Q. Were these funds forthcoming for this [109] project.

A. Yes, sir.

Q. Were those training films produced?

A. Yes, sir.

Q. Approximately how many of them were there?

A. There were approximately 30 or 40. I can't remember.

Q. Was the nature of these films secret?

A. Pardon me?

Q. Were they classified as secret information?

A. These are fairly classified. I wouldn't discuss them.

Q. In any event, they were actually filmed and delivered, is that correct?

A. They were delivered and paid for.

The Court: In 1948, or thereafter?



(Testimony of Maurice P. Koch.)

A. Thereafter, yes, sir—in 1948 or thereafter.

Q. (By Mr. Fink): You have in mind after January 1, 1948, or after the close of 1947, which is our year in question. They were after that?

A. Yes.

Q. By the way, in your experience in connection with the film business and the financing of film activities, what, in general, are the time problems that are involved?

Mr. Gillard: I object to the question as ambiguous, if the Court please.

The Court: I think it is.

You can reframe it, Counsel. [110]

Mr. Fink: I guess I am a little bit confused by it, myself, your Honor. I am sorry.

Q. In your experience in the financing of films and the setting up of the transaction necessary to produce films, what time delays have you generally experienced?

The Court: From what to what?

Mr. Fink: Well, in the negotiations, preparation leading up to the actual date of the turning of cameras.

Mr. Gillard: If the Court please, I will object to it as incompetent, irrelevant and immaterial. He can ask for the particular sequences involved in the activities Mr. Koch was engaged in, but as to his general experience, that is a little remote.

The Court: That is right. There may be a lot of irrelevance involved in it.

Mr. Fink: That is true. I will withdraw the question.

(Testimony of Maurice P. Koch.)

Q. Mr. Koch, I think you told us yesterday that prior to the actual filming of the picture, "Copacabana," you spent some three weeks at Goldwyn Studios in Los Angeles, or Hollywood.

A. Yes, sir.

Q. I wonder if you could tell us, just what did you do during that three-weeks period—not what was said or done by other people; just what did you do during that three weeks period? [111]

A. I went over the budget of the pictures—of the picture.

Q. What do you mean by "budget"?

A. Well, the budget that allocated so many dollars for costumes, so many dollars for sets, so many dollars for so many dance numbers, floor numbers, on the show. In other words, the budget of the picture, the dollars and cents spent in making the entire picture, which included not only labor, but materials.

Q. In reviewing this budget during that three weeks that you were in Los Angeles did you do anything in connection with the budget?

A. Yes, sir.

Q. What did you do?

A. Well, I visited all of the sets. I went over the sets with the departmental heads. We discussed the costs of these various sets. We cut expenses here; we added more onto other departments.

Q. What do you mean by you "cut expenses here"? Will you give us an example of that?

A. Well, yes. The budget was a little high, and

(Testimony of Maurice P. Koch.)

when we determined to make this picture we allowed so much for the burdget for preproduction, and we knew what we were going to get from the bank and Standard Capital, and we had to keep more or less in line with that budget, for if we went overboard we might be in trouble with the bank or with Standard [112] Capital, and if the picture cost us more money than we figured it would cost us, we would not make what we figured we would make on the picture.

Q. Did you change the amounts of money allotted for any particular sequence in the picture?

A. Yes, sir.

Q. Can you give us an example of that?

A. Yes. We had—well, I will put it to you this way: We had very good people down there, and they are artists. They have a tendency, on sets, to go overboard. Cost sometimes doesn't mean too much to them, but to the producer it means a lot. We got the people in that department together—Sam Coslow, we got Dave Hersh—and we went out on the sets, and we cut the costs of manufacturing these particular sets. We made some of them a little less elaborate; we made some of them a little more elaborate. But we went over these figures to try to keep the costs on these sets within the budget, and the same thing applied to costumes for the girls. They had a lot of dance routines there—they must have had 30, 35, 40, or more there. We cut those down considerably.

(Testimony of Maurice P. Koch.)

Q. What was the occasion for cutting them down?

A. Well, it cost too much money. As I said before, we were trying desperately to stay within the budget as much as we could.

Q. You told us you talked to the individual department heads. [113] Did you make inquiry with regard to the cost of the various elements that were to make up the picture? A. I did, sir.

Q. Did you have occasion to talk to the writers?

A. Yes, we had meetings with the writers. We rewrote that story several times. We had about 11 writers altogether on this picture, "Copacabana," and we had a lot of meetings on this, and we really had to cut it down, because the costs there were getting a bit exorbitant. We had meetings, decided what we were going to do, and we limited the story to a limited amount of writers, letting some of the writers go, and finally made a decision of how it was going to be and what final costs we would eventually wind up with.

Q. Did you read the materials that were prepared from day to day? A. Yes, sir.

Q. Prior to this three weeks stay in the studio had you been to the studio on previous occasions during the preparation of this picture for filming?

A. Yes, I had.

Q. On how many occasions?

A. On many, many occasions.

Q. During the course of the photography, dub-

(Testimony of Maurice P. Koch.)

bing, and the cutting of that film, did you also return to Goldwyn Studios from time to time? [114]

A. I did. I saw the films shown the next day of what was taken the previous day.

Q. Did other members of your family, or your partnership, also go down to Hollywood in the course of the filming of this picture and attend at the studio? A. That is right, they did.

Mr. Fink: I believe that is all at this time of this witness.

The Witness: Do you want these, Mr. Fink?

Mr. Fink: Excuse me. These are dated in 1948, your Honor, so I will not offer them at this time.

### Cross-Examination

By Mr. Gillard:

Q. Mr. Koch, as I recall your testimony, your first testimony in this case, the start of your activities was sometime before this "Copacabana" venture, with reference to several matters which, as I believe you expressed it, did not jell, is that correct? A. That's right.

Q. And I understand that along in that period of time it came to your attention from your attorney, Mr. Grupp, that the existing partnership agreement in the Koch family was insufficient to cover any motion picture financing activities on your part, and that pursuant to his suggestion an amendment was made to the partnership agreement? A. That is right. [115]

Q. And that amendment, which is Exhibit 2 in

(Testimony of Maurice P. Koch.)

evidence in this case, was dated the 23rd day of October, 1944?      A. That is right.

Q. And the reason for that amendment, Mr. Koch, was that the original partnership agreement required that you spend all of your time in the luggage manufacturing business, and if you did not so spend all of your time in that business your partnership interest was subject to forfeiture?

A. No, sir, I do not believe that is true.

Q. I just asked you the question.

Mr. Fink: Just a moment, please.

I am a little late, your Honor, but may I move to strike the answer for the purpose of the objection?

The original agreement, as well as the amendment to the partnership, speak for themselves, your Honor. I do not think the witness should be called upon to state what they mean or say.

The Court: I think they do speak for themselves. However, counsel may interrogate about them if there is any doubt about what they say.

Q. (By Mr. Gillard): Wasn't the reason for the amendment to the partnership articles, Mr. Koch, the advice of Mr. Grupp that under the existing partnership articles your interest would be subject to forfeiture because you were not entitled to spend any time except in the luggage manufacturing business? [116]      A. That is not true.

Q. What was the reason for that amendment, Mr. Koch?

A. One of the main objections—I mean, one of the main reasons to draw up a new agreement was

(Testimony of Maurice P. Koch.)

there is a clause in that partnership agreement that says that if any of the partners are absent from the business—I don't remember whether it is 30 or 60 days; I believe it is 60 days—that for \$1,000 we could pay that partner off, and he shall never receive any other remuneration from the business. And it looked to me like we were going into other ventures. The luggage business was—we had been in it before, and we felt after the war the luggage business would sort of slide, which it finally did, and we thought we wanted to get into some other business where we could make some money, and it might take more of my time than what the contract called for, and that is one of the most pertinent reasons Mr. Grupp suggested that we draw up another contract, so there would be no difficulties in the future.

The Court: Mr. Gillard, when you ask that a document be identified, of you will, for the record, say what it is, so the record shows what is—just briefly.

Mr. Gillard: Will you mark for identification, if the Court please, document dated October 10, 1951, notarized by Maurice P. Koch October 15, 1951?

The Court: That is all right. [117]

Mark it Government's Exhibit A for identification.

(The 24-page tax protest referred to was marked Defendant's Exhibit A for identification.)

(Testimony of Maurice P. Koch.)

Q. (By Mr. Gillard): Preliminarily, Mr. Koch, I will hand you Plaintiffs' Exhibit 1, which is the original partnership agreement, and calling your attention to the last paragraph on page 3 thereof, will you read that, sir? A. "It is further"—

The Court: Just read it to yourself.

A. Pardon me (perusing document.)

Yes, sir. I read that.

Q. (By Mr. Gillard): The original partnership agreement provides, does it not, Mr. Koch:

"It is further understood and agreed that all of said parties hereto shall devote all of their time to the interests of the said business and for the benefit thereof." A. That is right.

Q. Wasn't it in connection with that provision that Mr. Grupp advised you that your activities in connection with the motion picture financing were in violation of that agreement?

A. That, and the previous statement that I made. I am not familiar with the entire contract at the present time, but the thing that I told you about, the 60 days, is very prevalent in my mind. [118]

Q. I will show you Defendant's Exhibit A for identification and ask you if that is a document which you executed in October, 1951?

Mr. Fink: I will stipulate the witness signed it. It may go right into evidence.

Mr. Gillard: I do not desire to offer the whole document at this time, if the Court please. I want to direct the witness' attention to certain portions of it as we go along.



(Testimony of Maurice P. Koch.)

Mr. Fink: May I be heard?

The Court: There is nothing before the Court. You stipulated he signed it. That is all, so far, we have reached.

Mr. Fink: If I may, your Honor?

The Court: Let us go on to the next question, please.

Q. (By Mr. Gillard): Subsequent to the date of the execution of the amendment to the partnership articles, in October of 1944, were your activities in connection with the motion picture field pursuant to the amended articles of partnership, those amended articles of partnership?

A. I didn't get the beginning of that. I can't hear you very well, either.

Q. Were all of your activities in connection with your motion picture activities subsequent to October, 1944, pursuant to the terms of the partnership agreement as amended on that date?

A. Did you say prior to that—— [119]

Q. Subsequent—after that time, sir. Were your activities in the motion picture field conducted pursuant to the authority contained in the amended partnership articles of October, 1944?

A. Yes, they were in line with the new agreement.

Q. You got your authority to act in connection with the motion picture business from those articles, did you not, sir?           A. Yes.

Q. And all of your activities were pursuant to

(Testimony of Maurice P. Koch.)

the authority contained in that amendment of October, 1944?      A. I would say so, yes.

Q. And, Mr. Koch, will you tell us, during the year 1946, what were your activities in connection with the luggage business of the Koch partnership?

A. During the year 1946?

Q. And 1947.

A. I was the general manager of the firm. I did most of the procurement. I did most of the selling. Ran the firm as general manager.

Q. I gather from your answers to Mr. Fink's questions your two brothers were in the manufacturing end of the plant?

A. That is right, sir.

Q. And your sister was the bookkeeper?

A. That is correct.

Q. Outside of that were the business affairs of the [120] partnership, as far as the luggage manufacturing was concerned, in your hands?

A. That is right.

Q. In addition to all the financing and all procurement you also did all the selling?

A. That is right—not all the selling; part of it. We had some commission men out selling to the post exchanges and ship's stores.

Q. Were there any salesmen employed by H. Koch & Sons outside of yourself?

A. No, sir.

Q. Were those commission men you referred to employed during 1946?      A. Yes, sir.

Q. Are you certain, Mr. Koch?

(Testimony of Maurice P. Koch.)

A. Yes, sir.

Q. They were employed in 1947?

A. Yes, sir.

Mr. Gillard: By stipulation I will offer in evidence the 1946 partnership return of H. Koch & Sons, a photostatic copy thereof.

The Court: Exhibit B.

(The partnership income tax return for 1946 referred to was marked Defendant's Exhibit B in evidence.)

Mr. Gillard: I offer also the 1947 partnership return [121] of H. Koch & Sons.

The Court: Exhibit C.

(The partnership income tax return for 1947 referred to was marked Defendant's Exhibit C in evidence.)

Mr. Gillard: I offer the individual tax return of Maurice P. Koch for 1946.

The Court: Exhibit D.

(The individual income tax return for 1946 referred to was marked Defendant's Exhibit D in evidence.)

Mr. Gillard: I offer the individual income tax return of Maurice P. Koch for 1947.

The Court: Exhibit E.

(The individual income tax return for 1947 referred to was marked Defendant's Exhibit E in evidence.)

(Testimony of Maurice P. Koch.)

Q. (By Mr. Gillard): Mr. Koch, what area did your selling activity involve?

A. The 12 Western States.

Q. The commission sales that you referred to, do your books and records reflect what portions of the gross sales of the partnership were the result of the activities of those commission men?

A. Yes, those records will speak for themselves. They are in the books.

Q. You do not know at the present time what they are, is that so? [122]

A. No, sir.

Q. I will show you Exhibits B and C, which are the partnership returns for 1946 and 1947, and calling your attention to the fact that in the list of expenses for 1946 no expense is shown for commissions paid, whereas there is an item of \$28,000 listed as commissions paid for 1947. Does that refresh your recollection as to whether or not commission men were employed in 1946?

A. That is right; they must have started in 1947, then. I am sorry. I was speaking from memory.

Q. What was the gross revenue of the partnership for 1946, Mr. Koch?

A. The gross revenue—well—the cost of goods sold——

Mr. Fink: May I interrupt, Mr. Koch?

I object to that upon the ground it is immaterial what the gross revenue is, your Honor.

The Court: The tax returns are in evidence. I take it any part of them——

(Testimony of Maurice P. Koch.)

Mr. Fink: Then they would speak for themselves, your Honor.

The Court: Yes, they do, but I take it he can ask that. It may be preliminary. I don't know.

Q. (By Mr. Gillard): The gross sales for the partnership for 1946, Mr. Koch, were how much?

A. 1946 were \$540,375.82. [123]

Q. And I gather from your testimony you were responsible for all those sales? A. Yes, sir.

Q. What was the gross revenue, gross sales for 1947?

A. 1947 it says "Revenues—Net," here. Is that sales?

Q. Gross sales would be the top figure, I suppose. A. \$555,532.46.

Q. Do you know what part of that was the result of your activities as a salesman for H. Koch & Sons?

A. I couldn't tell you offhand. I would have to subtract the amount of sales that were paid commission men from that total, and the balance would be mine.

Q. During 1946 and 1947, Mr. Koch, were you interested in any other business activity besides luggage sales and motion picture financing?

A. Yes, sir.

Q. What business was that?

A. Oh, besides motion picture financing?

Q. Yes, sir.

A. I was interested in a fiber-glass plant.

Q. What was that?

(Testimony of Maurice P. Koch.)

A. I was interested in a fiber-glass plant.

Q. As a part owner?

A. No, sir, not at that particular time, but I finally wound up buying it. [124]

Q. What year was that?

A. That was the year of—it could have been the end of 1946 or the first part of 1947. I can't remember.

Q. Where was that fiber-glass plant located, sir?

A. In San Rafael. I invested a lot of money. I helped finance the company. And I finally wound up buying the plant.

Q. This was in connection with the shift in the luggage manufacturing business to a fiber-glass product?

A. That is right, sir.

Q. When did you first start to become interested in that fiber-glass plant?

A. I believe it was around 1946.

Q. With whom were you dealing for the purchase of that property?

A. With whom?

Q. Yes, sir.

A. Well, I finally bought it from a Bankruptcy Court.

Q. In connection with that you had to examine the plant that was there?

A. Yes, sir.

Q. Go over the books and records of the company?

A. No.

Q. You did not do that?

A. No, sir. I owned most of the molds in the company, and the things that they left were practically of no consequence. [125] I just wanted to

(Testimony of Maurice P. Koch.)

make sure no one else got it, because we had spent a lot of money there developing.

Q. How much time did you spend in 1946 investigating and making up your mind about the purchase of that fiber-glass plant?

A. My brothers did most of the investigating. It was mostly engineering, developing, and things like that.

Q. You made the purchase toward the end of 1946?

A. I believe the purchase was made in 1947. I have records on that.

Q. Were you interested in any other business in 1946 and 1947?

A. Motion pictures.

Q. Is that all, sir?

A. I can't think of anything right now.

Q. Weren't you actively engaged in the partnership with Farilla & Sons, Mr. Koch?

A. Oh, yes; yes, sir. I was a partner in Farilla & Sons from 1946 to 1947. I forgot all about that.

Q. You were active in the running of that business, were you not?

A. Yes, sir; I was active at the beginning of the business for about six months—helped them out; maybe six months to a year.

Q. What did you do in connection with A. Farilla & Sons, or [126] Farilla & Sons?

A. I helped them in the buying, and gave them a lot of knowledge of merchandising, and I helped them in financing purchases, credits, and things

(Testimony of Maurice P. Koch.)

like that. We did help them in the financing of the business.

Q. As a matter of fact, it was by virtue of your experience and your credit with Koch & Sons that you were primarily of value to the Farilla partnership?

A. Let me explain that. Mr. Farilla was a very good friend of mine. I didn't go into that venture with the intentions of making any money. Mr. Farilla, when he was discharged from the Army, he came down to San Francisco and spent over three months in my house with his wife and child. He had some office up in Portland and Seattle. I knew Frank for about 30 years, and I wanted him to settle down in San Francisco. So I tried to set him up in business. I actually set Farilla up in business in San Francisco. As a matter of fact, when he went into business all that both of us put in was about \$2,000 each. It wasn't very long before we got that out of the business.

Q. That \$2,000 was hardly sufficient to run a business of the size that the Farilla partnership developed into, was it, Mr. Koch?

A. At that particular time, in 1946, money was turning over fast, and, by golly, we got paid for merchandise in 1946 before [127] we delivered it, practically speaking, and we rolled that money around.

Q. What did you do for the Farilla partnership, sir?

A. Well, I gave Farilla a lot of advice. I helped



(Testimony of Maurice P. Koch.)

him in the merchandising business and I helped him in the buying.

Q. This was continuous throughout the year 1946?

A. Well, practically through the year 1946, yes.

Q. Your return for those activities was substantial, was it not, Mr. Koch?

A. My return—you will find my tax on my return for the profits that we received, yes, sir.

Q. For the year——

A. 1946 and 1947. I got out in 1947.

Q. In 1946 you received as your share of the Farilla partnership \$10,432?

A. Whatever is there.

Q. In 1947 you received \$9,511?

A. The record speaks for itself, yes.

Q. Now, you first heard about the “Copacabana” deal from whom?

A. I first heard about the “Copacabana” deal from Dave Sebastian.

Q. Do you remember when that was, Mr. Koch?

A. That was in the early part of 1946.

Q. Do you know the date, sir?

A. No, sir. [128]

Q. Was it before or after the Beacon Pictures Corporation was formed?

A. I believe it was—I can’t tell you exactly, but I believe it was before it was formed. I am not sure.

Q. Did you have anything to do with the formation of Beacon Pictures Corporation?

(Testimony of Maurice P. Koch.)

A. Personally, no.

Q. That was formed by whom, sir?

A. Beacon Pictures Corporation was formed by Hersh, Coslow—I will tell you who the stockholders were, there—was that your question?

Q. First, who formed it?

A. I think Hersh and Coslow formed it, or Hersh, Coslow, Batchelor, Monte Proser and George Frank. I couldn't tell you who formed it.

Q. Did any of those gentlemen discuss with you the advisability of forming the Beacon Pictures Corporation?

A. I talked to Hersh and I talked to Coslow, and as part of our deal we advanced them money to participate in the stock of Beacon Pictures Corporation. I don't know whether they put the money in there to form the corporation, or whether they put the money in there to buy the stock. I imagine they bought stock. In this picture business it doesn't make any difference. The corporation might have been dormant for a long time, but if it didn't have any money, it didn't have any [129] vehicle to move with, and the money was the thing that counted. So it was formed or it was not formed. I can't remember, now, after ten years.

Q. Do I understand your testimony correctly, Mr. Koch, that you had no part in the advice, or other discussions—any advice or discussions leading up to the formation of Beacon Pictures Corporation?

(Testimony of Maurice P. Koch.)

A. I didn't have anything to do with the Beacon Pictures Corporation.

Q. I believe you testified on direct examination that that first check that was sent by you on behalf of the partnership for \$15,000, out of that check \$10,000 was for the purpose of incorporating Beacon Pictures Corporation.

A. I just told you a few moments ago that that \$10,000 that we gave Hersh, that we sent down to Mr. Sebastian, was for the stock in the corporation, for Hersh and Coslow, and I don't know whether they formed the corporation, bought stock, or if that was part of the deal, but that \$10,000 was for stock for Hersh and Coslow, for which they were to pay back the \$10,000 plus an interest in the picture.

Mr. Fink: We have a stipulation between counsel that the deposition, which was rather hurriedly prepared—only two days given to the reporter last week for that purpose—may be used without signature with the same effect as though signed and acknowledged. [130]

Q. (By Mr. Gillard): Do you recall you were in my office about a week ago today, Mr. Koch, and I took your deposition in this matter?

A. That is right.

Q. Do you remember, sir, at that time I asked you with reference to this \$17,500?

A. Yes, sir.

Q. Do you recall at that time that you told me, on page 31 of the deposition:

(Testimony of Maurice P. Koch.)

“A. All right, then, that was split into two checks. \$10,000 of that was given to Hersh and Sam Coslow to form the corporation, and \$7,500 of that was given to Hersh and Sebastian for immediate expenses down there to get the thing going, get the picture going.”

Do you recall that?           A. I did——

Mr. Fink: May I request, your Honor, that the usual foundation be laid; that the witness be shown the deposition and given a chance to read it?

The Court: All right.

The Witness: I remember that. That is right.

The Court: Just a moment. There is no question pending now.

Q. (By Mr. Gillard): Was that your testimony at that time, [131] sir?

A. Yes, sir. I would like to explain that. This transaction occurred about ten years ago. When I went in to take this deposition I was giving you all the answers that I could honestly, from memory. Since then I have refreshed my memory and found out it was not given to them to form the corporation, but it was given to them to purchase some stock in the corporation, and that is of record. I was answering all of these questions—but it did go into the corporation, the money did go into the corporation, and the corporation was there.

Mr. Gillard: I will offer in evidence a certified copy of the Articles of Incorporation of Beacon Pictures Corporation filed in the office of the Sec-

(Testimony of Maurice P. Koch.)

retary of State on April 8, 1946, as defendant's next in order.

The Court: Exhibit F.

(The Articles of Incorporation referred to were marked Defendant's Exhibit F in evidence.)

The Court: Is it convenient to take a recess at this time, Counsel?

Mr. Gillard: Yes, your Honor.

The Court: We will take a short recess.

(Recess.)

The Court: Proceed.

Q. (By Mr. Gillard): Mr. Koch, these first checks that were [132] issued in this situation, the one for \$15,000 and the one for \$2,500, were the funds of H. Koch & Sons, the partnership, is that correct? A. That is correct.

Q. And you have testified, now, that \$10,000 of that went to the partnership of Hersh and Sebastian, and then they used that to buy an interest in Beacon Pictures Corporation?

A. No, sir; I testified that that \$17,500 was split up into two parcels. The \$10,000 went to Hersh and Sam Coslow for procuring their stock in Beacon Pictures Corporation, and the \$7,500 went to Hersh and Sebastian for expenses in getting the show on the road.

Q. The loans were made by H. Koch & Sons to whom?

(Testimony of Maurice P. Koch.)

A. The checks speak for themselves. I believe the check was made out to David Sebastian. I am not sure. I would have to look at them.

Q. That is correct, sir. At that time was Sebastian in the partnership?

A. Sebastian had a partnership with Hersh.

Q. These moneys were advanced to David Sebastian and not to Sebastian and Hersh, is that correct?

A. The moneys were advanced to David Sebastian; he turned them over to the partnership, and I believe the partnership gave them to Hersh and Coslow. That is the \$10,000.

Q. As far as you were concerned, the transaction was with [133] David Sebastian and H. Koch & Sons, and was not concerned, therefore, with what David Sebastian did with that money, is that correct?

A. No, sir. Sebastian and Hersh were actually working for me in this deal, and they were looking out after that money, and I was to receive interest in the picture. I was participating in the picture for the money that I put into the Hersh and Sebastian, or the Hersh-Coslow, or Beacon Pictures—as a matter of fact, I think I wound up to be the biggest participator in the entire picture. I had more interest in the picture than any individual.

Q. Your sole interest or remuneration for that money was to come to you from Sebastian or Sebastian and Hersh, was it not?

(Testimony of Maurice P. Koch.)

A. No; we had notes from Beacon Pictures Corporation, too.

Q. I am not referring to the \$80,000 represented by notes to the Beacon Pictures Corporation, Mr. Koch. I am referring to this \$17,500 which was represented by these two checks to David Sebastian.

A. Yes. When the corporation would have been liquidated at the end of the picture we were to receive—we were to have the \$10,000 that we gave Hersh and Coslow back, plus an interest—plus part of their interest in the picture, and the same thing applied to the \$7,500 from Hersh and Sebastian.

Q. Are you testifying that you considered the \$17,500 loaned [134] to David Sebastian was a direct loan by you to Beacon Pictures Corporation?

A. Well, you speak of a corporation, or a picture corporation. A picture corporation is nothing more—and this is common in the picture business, and I have been related to the picture business for 25—

The Court: Will you answer the question?

Read the question.

Then answer it, and then you may explain.

(Question read by the reporter.)

A. Well, it wasn't loaned to Beacon Pictures Corporation. But can I explain this?

Q. (By Mr. Gillard): The loan was to David Sebastian, is that correct?

A. It was to Hersh and Sebastian.

(Testimony of Maurice P. Koch.)

The Court: You may explain it.

A. The corporations in a picture business is merely a vehicle to move one picture, and when the picture is through the corporation is liquidated.

Now, we deal mostly with individuals, and as far as we were concerned, **H. Koch & Sons, it didn't** make much difference whether we gave money to Hersch and Sebastian, or Hersch and Coslow, or Beacon Pictures Corporation. It was practically all one part of one money for one purpose in mind, and that was to make a picture called "Copacabana," and we were dealing [135] with individuals and not a corporation, but the corporation was merely the legal vehicle by which the picture moved, and borrowed money from the Bank of America and Standard Capital and various other things to complete the picture and release it through various releases as well as United Artists.

I hope I made myself clear.

Q. (By Mr. Gillard): Mr. Koch, subsequently, after the \$17,500 transaction, there was advanced by the partnership directly to Beacon Pictures Corporation \$50,000, and then \$30,000 represented by the checks and the notes which are in evidence, is that correct? A. That is correct.

Q. And those were direct loans by the partnership to Beacon Pictures Corporation?

A. That is correct.

Q. And that was the sum of money, that \$80,000, for which you subsequently sued the Beacon Pictures Corporation, is that correct?



(Testimony of Maurice P. Koch.)

A. Not that \$80,000, no, sir. We sued Beacon Pictures Corporation for \$75,000 in our name and \$5,000 in R. J. Haller's name.

Q. That is a total of \$80,000?

A. That is right, sir, but it wasn't that particular \$80,000. I mean, if you want to put all the moneys together, I can't pinpoint it on that \$80,000, because there was \$97,500 in the [136] whole deal, and we only sued for \$80,000.

Q. What evidence of indebtedness did you have upon which you sued Beacon Pictures Corporation, outside of the two notes in evidence, one for \$50,000 and one for \$80,000?      A. \$30,000.

Mr. Fink: To which we object on the ground there is no foundation laid that Beacon Pictures was ever sued, based upon any evidence of indebtedness.

The Court: He may answer if there were not.

The Witness: I don't remember suing them. They went into bankruptcy, I believe. We never sued them.

The Court: A moment ago you said you sued them.

A. No; I meant—he asked me, and confused me—pardon me, sir—Mr. Gillard asked me and confused me. We put in a claim in bankruptcy, is what we did, and the record speaks for itself. It is there.

Q. (By Mr. Gillard): You did not sue Beacon Pictures Corporation?      A. No, sir.

Mr. Gillard: May this document, which is a judg-

(Testimony of Maurice P. Koch.)

ment dated in June of 1949, be marked for identification?

The Court: Exhibit G for identification.

(The default judgment referred to was marked Defendant's Exhibit G for identification.)

Q. (By Mr. Gillard): I will show you Exhibit G for [137] identification, Mr. Koch, and ask you if this refreshes your recollection as to whether you sued Beacon Pictures Corporation.

A. Well, I have forgotten this completely, because I never was there at the trial.

Q. Does that refresh your recollection, sir?

A. I just can't remember suing them, but I guess it must have been. It says here that we sued, and since Beacons never showed up, they gave us judgment.

Q. That is correct, sir?

A. I didn't remember that.

Q. I will show you a transcript of your deposition taken last week, on page 38 thereof, and ask you to read your answer at the bottom of that page.

A. (After perusing deposition.) This confused me.

Q. Let me ask you a question, Mr. Koch.

A. Yes, sir.

Q. At that time did I ask you the question as to whether or not the basis of the suit—

The Court: Read the question.

Q. (By Mr. Gillard, reading): "Q. Mr. Koch,

(Testimony of Maurice P. Koch.)

this suit was—the basis of this suit was two promissory notes signed by Beacon Pictures Corporation, each in your favor, one for \$50,000 and one for \$30,000, wasn't it? [138]

“A. That is correct.”

Mr. Fink: Will you read on, Counsel.

Q. (By Mr. Gillard): Is that the question and the answer?

A. Yes, sir. May I explain that, please? In my mind I know that we filed for the money that was coming to us, in bankruptcy, and I didn't know whether that was a suit or whether it was filed in bankruptcy as money that was coming back to us, and I guess I am confused relative to the suit and the bankruptcy, but we did put in a claim for it either way.

Q. You are referring now to the second document in Exhibit G, which is the claim signed by you on July 20, 1949, in the matter of Beacon Pictures Corporation.

A. That is my signature. That is what I thought we had. Is that the bankruptcy?

Q. Yes, sir.

A. That is the one I thought.

Q. Looking at those two documents together, Mr. Koch, is your recollection refreshed that you sued Beacon Pictures Corporation for \$80,000; that the claim included some \$15,000-odd of interest, making a total claim of \$95,319; that you filed that claim in bankruptcy and supported it with a copy of the judgment secured which you have in front of you?

(Testimony of Maurice P. Koch.)

A. Evidently that is what was done here.

Mr. Gillard: I will offer those two documents in [139] evidence, if the Court please.

The Court: They may be admitted and take the same letter.

(The two documents formerly marked Defendant's Exhibit G for identification were now received in evidence and so marked.)

Q. (By Mr. Gillard): Mr. Koch, you testified extensively as to some activities on your part in the latter part of 1946, when you said they were having difficulty with this "Copacabana" film. At that time your sole interest in this matter was as an investor in Beacon Pictures Corporation as represented by the monetary transactions we have already discussed, is that correct?

A. Well, I was more than an investor. I actually participated in "Copacabana."

Q. You mean in the making of the picture?

A. Yes, sir.

Q. I gathered from your testimony on direct examination that you were sort of an advisor to the producer, to the cameraman, to the property men, and to the scenery makers, and to the financial men, and everybody concerned with that picture, is that right?

A. I didn't say I was an advisor.

Mr. Fink: Just a moment, please.

I object to the question, your Honor, on the ground it is [140] argumentative.

The Court: Sustained.

(Testimony of Maurice P. Koch.)

Mr. Fink: Thank you.

Q. (By Mr. Gillard): At the time that you went down there, you testified on direct examination that you told Mr. Fink to file a suit against the Bank of America for a million dollars.

A. That is right, sir.

Q. Did you have any contracts or contractual obligations with the Bank of America?

A. Personally, no.

Q. When you were talking about the fact that you asked Mr. Fink to sue the Bank of America, you were talking about on behalf of Beacon Pictures Corporation?

A. That is right.

Q. And your sole interest at the time in seeing that the Bank of America and Standard Capital came through with their loans was for the purpose of protecting the pre-production money which you had already advanced, is that correct?

A. Well, that and a lot of other things.

Q. What other things?

A. Well, my main purpose of going down—my main purpose of making sure that we got the bank money was not only to protect the money that we had put in Beacon Pictures Corporation but to see that the picture was made so that we could make a dollar off of it. After all, I had spent a lot of time in [141] promoting this thing and we not only wanted to get our money out of it but we wanted to get a profit.

Q. Prior to the end of 1946, at the time "Copaca-

(Testimony of Maurice P. Koch.)

bana" was started to be filmed, what had been your experience in making motion pictures, Mr. Koch?

A. Well, I have seen a lot of pictures, I have been on a lot of sets in the last 25 years. My father-in-law was a pretty large person in motion pictures.

Q. I asked you what your experience was.

A. I had been down in Hollywood with my father-in-law when he was alive. We had discussed a lot of pictures backwards through 1944. We had gone into a lot of deals, and as far as the business ability of making motion pictures and promoting motion pictures, there is not a lot of difference in that business and merchandising as there is in other businesses. You can hire artists, you can hire writers, you can hire directors, you can hire producers, and if you have got a pretty good knowledge of what is going on, you can make a picture.

Q. Now, sir, to go back to my question, what is your personal experience in making motion pictures prior to this time?

A. In making motion pictures?

Q. Yes.

A. Well, I never actually made one myself I don't know anyone that has. [142]

Q. Were you ever an employee of a company that did make a motion picture prior to this time?

A. No, sir.

Q. Were you ever on anybody's payroll in connection with the making of a motion picture prior to that time?

A. No, sir.

Q. The next corporation you testified to was the

(Testimony of Maurice P. Koch.)

Ambassador—is that Ambassador Pictures Corporation?     A. That is right.

Q. Or Ambassador Production, Inc.?

A. We called it both. They are Ambassador Productions Corporation.

Q. The idea for the formation of that corporation came from Mr. Fink, did it?

A. Well, not exactly. I talked to Mr. Fink. We were talking about a group of pictures that we were going to make with Al Green, and I talked to Mr. Fink and told him I thought it would be a good idea to get a corporation up so we would have a vehicle which to roll on. After all, I had been in one picture “Copacabana,” and I had loaned money.

Q. The moneys that were put into the Ambassador Production, Inc., was your personal money, was it, Mr. Koch?

A. At that particular time it came out of my personal funds.

Q. Checks were drawn upon your personal account?     A. Yes, sir. [143]

Q. And it was not a partnership loan, was it, Mr. Koch?

A. Well, the partnership was a little short at the time, so I advanced the money personally.

Q. It never was a partnership transaction, was it?     A. Yes, sir.

Q. Was it reflected as such on the books of the partnership?     A. No, sir.

Q. In any way, shape or form?

A. No, sir.

(Testimony of Maurice P. Koch.)

Q. You talked on direct examination in connection with a total of \$25,000.00 advanced to Ambassador Pictures Corporation? A. Yes, sir.

Q. Was that \$25,000.00 all your money?

A. No, sir.

Q. How much of it was your money?

A. \$17,000.00.

Q. How much of it was the money of somebody else?

A. \$8,000.00 came from Producers' Finance Corporation.

Q. And that was advanced by Producers' Finance Corporation to Ambassador Productions, Inc.? A. Right, sir.

Q. A corporate loan from Producers' Finance to Ambassador Productions?

A. That is right, sir.

Q. Do you know when you received your stock in Ambassador [144] Productions?

A. I don't know exactly, but I think you have a record of it there. It was in 1947, I think. I am not sure.

Q. The permit to issue stock, Mr. Koch, is dated April 16, 1947. Would that refresh your recollection as to when you purchased any stock in that corporation?

A. I gave Max Fink a check for the stock at the Friar's Club in Hollywood, and it was some time later that he mailed me the stock of the corporation. I believe you have some letters that we put in evi-



(Testimony of Maurice P. Koch.)

dence that will give you the date. I can't give you the date.

Q. The check you refer to is a check for \$7,000.00?

A. The first check I gave him was for \$7,000.00. That was for the stock of the corporation.

Q. That is Exhibit No. 30. That is the check of December 3, 1947, is that correct?

A. If that is for \$7,000.00, yes.

Q. And that was the only stock that Ambassador Productions issued, is that correct?

A. That is correct. I had all of the stock.

Q. And you were the sole stockholder?

A. I was the sole stockholder, yes, sir.

Q. And from that point on all your dealings with Ambassador Productions, Inc., were as the sole stockholder of Ambassador Productions, Inc., is that correct? [145]

A. Yes, I was the sole stockholder.

Q. All of the testimony that you have given yesterday and today with reference to the affairs of Ambassador Productions, Inc., your participation in those affairs was as the sole stockholder of Ambassador Productions, Inc.?

Mr. Fink: To which I object, your Honor, on the ground it assumes facts not in evidence.

The Court: You have asked the question. He may answer it "yes" or "no."

The Witness: Would you rephrase that? That is taking in a lot of territory.

The Court: Read the question.

(Testimony of Maurice P. Koch.)

(Question read.)

The Witness: I don't know what he is talking about there.

The Court: Reframe your question. I wish you would rephrase that question.

Q. (By Mr. Gillard): Your interest in Ambassador Productions was as the sole stockholder, was it not, Mr. Koch?

A. Yes, I owned all the stock or the firm of H. Koch & Sons owned all the stock of Ambassador Pictures Corporation.

Q. And from that time on your dealings with reference to that corporation or on behalf of that corporation, you were acting as the sole stockholder thereof?

A. May I ask you, what do you mean?

Q. I believe you testified, Mr. Koch, with reference to [146] numerous affairs. You are more familiar with them than I am because I have just rough notes on them. I believe you have testified at length with reference to the affairs engaged in by Ambassador Productions, Inc.

A. That was "Hill of the Hawk."

Q. Is that the only matter that you were concerned with in Ambassador Productions, Inc.?

A. "Hill of the Hawk" was the only thing that Ambassador Productions owned, yes, sir.

Q. In your transactions with reference to "Hill of the Hawk," you were acting as the sole stockholder of Ambassador Productions, Inc.?

(Testimony of Maurice P. Koch.)

A. That is right. "Hill of the Hawk" only.

Q. That "Hill of the Hawk" was never produced, was it?

Mr. Fink: To which I object as being immaterial, your Honor. It so happens that what may have happened years later, including the present time, with regard to that property is not material to this case. I will be glad to go into it if counsel wants to go into it.

The Court: I think he can answer the question "yes" or "no." He has been asked about it already.

(The last question was read.)

The Witness: No, sir.

Q. (By Mr. Gillard): And you eventually sold your entire interest in Ambassador Pictures, both your stock interest and [147] whatever interest the corporation had in the picture, to Mr. Jack Cher-tok?

A. That is correct.

Q. The Producers' Finance Corporation was incorporated on October 20, 1947. You were one of the directors of that corporation, were you, Mr. Koch?

A. Producers' Finance? I am the president.

Q. You were one of the directors and then you became the president, is that correct?

A. I think I was always the president.

Q. And you were one of the original incorporators or directors named in the Articles?

A. I am one of the original incorporators, yes, sir.

(Testimony of Maurice P. Koch.)

Q. And you were immediately elected president of the corporation when the organization was formed, is that correct?

A. If that is the way they do it, that is what happened. But I am the president and always was. I am not too familiar with those things.

Q. With reference to Producers' Finance Corporation, you have testified to certain transactions?

A. Yes, sir.

Q. What were they, sir?

A. Well, Producers' Finance Company loaned money to Ambassador Pictures Corporation for the purpose of "Hill of the Hawk." We were to provide the money for the making of the picture [148] "Hill of the Hawk." We went into Government training pictures, about 30 or 40 of them.

Q. That was with Apex Films?

A. Apex Films, yes, sir.

Q. You testified something with respect to Monogram Pictures, did you not, sir?

A. Yes, we had quite a lot of dealings with Monogram, but we never did actually consummate a deal where we put up any money.

Q. Was that in connection with Ambassador Pictures or in connection with Producers' Finance?

A. That was not in connection with either one of them. There was no money put up. It was again people talking, myself and Monogram and Max Fink, and the people that were interested in making the pictures.

Q. Then to go back to Producers' Finance, the

(Testimony of Maurice P. Koch.)

deals that you have testified to that that corporation was interested in were the "Hill of the Hawk" and the Army training films with Apex Film Corporation?      A. That is right.

Q. Were those the only two?

A. Let's see. I have to think for a minute. There was "Hill of the Hawk," Ambassador Pictures; the Army training pictures. Right now I believe that is it.

Q. And in connection with all of those transactions, you were acting as the president of Producers' Finance Corporation? [149]

A. That is correct.

Q. Now, this Monogram picture situation that you testified with reference to, my notes show that you testified that was around the end of 1946 and some time early in 1947.      A. That is correct.

Q. That was the situation in which you explored for the purpose of trying to invest a sum of money but the deal fell through, is that correct?

A. That is correct.

Mr. Gillard: Would this be a convenient time to take a recess, if the Court please?

The Court: I would like to run to a quarter past 4:00, if we could.

Q. (By Mr. Gillard): I believe that there was a transaction that you testified to which was entered into on the same date that the Articles of Copartnership were amended. That was another partnership with about 15 people.

A. Yes, 15 or 25. That was the Producers' Syn-

(Testimony of Maurice P. Koch.)

dicate back in 1944. I promoted \$15,000.00 on that deal.

Mr. Fink: The agreement is in evidence. I think it is Exhibit 3, isn't it?

Mr. Gillard: Oh, yes, Exhibit 3 in evidence, an agreement of the Koch partnership dated the 23rd of October, 1944, between Dave Sebastian and about 13 or 14 other people.

Q. In that connection, Mr. Koch, you and the other persons [150] named in that agreement deposited the amount of money specified for each person with Mr. Grupp, did you?

A. That's correct.

Q. And the purpose of this agreement was that Mr. Sebastian was named the general manager of the partnership.

A. That is 1944. The agreement speaks for itself.

Q. Do you recall that he was the manager?

A. He had a lot to do with it, but I can't remember the exact title that was in there.

Q. The purpose of it was to have him explore a Sid Broad production, is that correct?

A. That is right.

Q. After exploring that for a few months, he determined no agreement could be reached with reference to that production, is that correct?

A. I went down to Los Angeles on that several times and I did a lot of exploring on that thing myself. It looked like we couldn't tie the ownership of the Mark Twain series down. One relative

(Testimony of Maurice P. Koch.)

had one, somebody else had another, and we were afraid of being sued after we made a picture by somebody who might have held title to that picture, and Sid Broad himself could not tie the title down. And we worked on that for months and months trying to tie the titles down, but we couldn't have done it. If we could have done it, we could have made the picture, the series, and so we gave everybody [151] their money back and we paid our own expenses on the deal. Everybody got 100 cents on the dollar back, but I promoted all the money for that picture.

Q. As a matter of fact, what happened was that Mr. Sebastian was charged with the responsibility of determining the advisability of investing this fund, was he not?

A. Well, I don't remember, but the way it turned out, I suggested that everybody get their money back. I can't remember the details in that deal. It was quite some time ago.

Q. I will refer you to Exhibit A for identification, Mr. Koch, and ask you to read that paragraph there with reference to the partnership.

A. Yes, that is in line with what I told you, only it says, "Mr. Sebastian reported to Mr. Grupp and me that he could not get the titles to the pictures."

Q. Let me read from this and ask you a question, Mr. Koch.

A. All right, sir.

Q. "Between the date of October 23, 1944, and January 18, 1945, the said David Sebastian periodically reported progress on his attempts to secure a satisfactory arrangement with regard to the Sid

(Testimony of Maurice P. Koch.)

Broad production to Maurice P. Koch or his attorney, Morris M. Grupp, and thereafter, some time during the middle of January, 1945, David Sebastian reported to Morris Grupp that he could not meet the conditions outlined by Maurice P. Koch to the investors in the Producers' Syndicate relative to the Sid Broad [152] productions and in line therewith on January 18, 1945, Morris M. Grupp as trustee returned the money to the investors." Is that correct?      A. That is right.

Q. So that this money that was put up was put up by a trustee of your selection, Morris M. Grupp, with instructions to hold it pending further determination of what should be done with it, is that correct?

A. No, not exactly. It doesn't work that way. I mean, if Morris Grupp decided to make apple carts out of the \$50,000.00, I think I would object strenuously to that.

Q. I do not believe that was my question, sir. I will withdraw that question. The contract speaks for itself. In any event, your money was put up by you in trust with Morris M. Grupp, the production fell through, and the money was returned to you, is that correct?      A. That is right?

Mr. Gillard: Except for a few tag ends, if the Court please, I think I am finished.

The Court: We will take a recess until 10:00 o'clock tomorrow morning. Remember the admonition heretofore given you. [153]



Wednesday, November 28, 1956—10:00 A.M.

MAURICE P. KOCH

a plaintiff herein, being previously sworn, resumed the stand and testified further as follows:

Cross-Examination  
(Resumed)

By Mr. Gillard:

Q. Mr. Koch, in the production of the moving picture "Copacabana," who was the producer?

A. The producer was Sam Coslow.

Q. What are the functions of a producer?

A. The function of a producer is to see that the entire picture is carried out, all the functions of the entire picture is carried out, to watch the budget, watch the costs, and keep a good eye on the director.

Q. He is, in effect, the over-all business manager of the picture? A. No, sir.

Q. Who occupies that function?

A. The executive. There is an executive producer.

Q. An executive producer? A. Yes, sir.

Q. He is the business manager of the affair, is he? A. Yes, sir.

Q. Well, the functions that you have described for the producer, like watching the budget, watching costs, and so on—— [154]

A. And watching the direction of the picture, the production of the picture.

Q. What would the associate producer do?

A. The associate producer would assist the pro-

(Testimony of Maurice P. Koch.)

ducer. In other words, the producer would be the manager of the picture and he would manage the picture, and the associate producer would assist him.

Q. Who was the director of the picture?

A. Al Green.

Q. What were the functions of the director?

A. Al Green, the director, would sit on every set and direct the actors that were at the camera, in front of the camera. He would take the picture, scene by scene, and try to explain and tell the actors exactly what they had to do at each scene.

Q. What other technical staff is there employed in the making of the picture? First, just by titles, Mr. Koch.

A. Well, they have writers, they have heads of costumes, they have heads of sets, they have a good cost accounting staff, they have got—well, they've got a lot of help all over the place, assistants—under the assistant producer.

Q. And that would include a regular force for the dance routines?

A. That is right. They would have teachers there to teach the girls how to dance. They would have dance instructors. They would have make-up artists there, head make-up artists [155] that were very big people.

Q. And property men?

A. Property men, yes, sir. They would have juicers there to take care of the electrical works, people that move things around.

(Testimony of Maurice P. Koch.)

Q. After the filming, they have people especially trained for the purpose of cutting and assembling the film?

A. That is right, they have filming editors and cutters. That is in the laboratory department.

Q. During the course of the transactions that you described to the jury with reference to these various productions, you considered your business was financing, didn't you, Mr. Koch?

A. My business was financing, but I was very much interested in the production of the picture because I had quite a bit of money in there.

Q. In connection with Producers' Finance Corporation, you referred to some dealings you had with Apex Films and some Army training films, is that correct?

A. That is right, sir.

Q. The contract for the making of those films was between the Army and Apex Films Corporation, was it not, Mr. Koch?

A. That is right, sir.

Q. Did you have any interest in Apex Films Corporation?

A. No, I had no interest in Apex Film Corporation outside of financing them on these [156] pictures.

Mr. Gillard: May this letter dated January 29, 1948, be marked as defendant's next in order?

The Court: In evidence? Is it being offered?

Mr. Gillard: By stipulation it may go into evidence.

The Court: Exhibit H.

(Testimony of Maurice P. Koch.)

(The document referred to was thereupon received in evidence and marked Defendant's Exhibit H.)

Q. (By Mr. Gillard): I will hand you Exhibit H, Mr. Koch. This is a letter, is it not, sir, from you, dated January 29, 1948, that is, from Producers' Finance Corporation, by M. P. Koch, Director, to Mr. Jack Chertok, setting forth in a preliminary form the basis of your understanding of advancing funds to the Apex Corporation?

A. That is right, sir.

Q. And the letter recites that Apex had these preliminary arrangements with the Army and was going to produce these films for the Army?

A. That is right.

Q. In that connection, then, the money that you testified about yesterday, this money from Pacific National Bank that you assisted in procuring, that million dollars of financing or thereabouts—

A. Yes, sir.

Q. —that money went to Apex Film Corporation?

A. That money went direct to Apex Film Corporation, yes, sir. [157]

Q. And you were interested in arranging that that money was advanced by the Pacific National Bank to Apex so that your loan could be to Apex and you could help to make a profit upon that, is that so?

(Testimony of Maurice P. Koch.)

A. That is right. I promoted the loan with Pacific National Bank.

Q. The details of the loan were finally worked out, I presume, between Apex and Pacific National Bank?

A. That is correct.

Q. The Pacific National Bank was interested in the credit standing of Apex Film Corporation, not in Producers' Finance Corporation?

A. Pacific National Bank was naturally interested in knowing all about Apex Film Corporation, and Jack Chertok—if I had not brought Mr. Chertok or Apex Film into our bank and he went in there cold, he would never have gotten the money.

Q. That may be, sir, but you were no part of the final loan transaction itself, were you?

A. No, not of the loan of the Pacific National Bank, not the loan that they made to Apex Film. Might I add that all of these things were predicated upon them getting the money for the picture and a loan being made.

Q. During the years 1946 and 1947 was any money loaned or invested by H. Koch & Sons, with the exception of money put into [158] "Copacabana"?

A. 1946 and 1947?

Q. Yes, sir.

A. Well, I think the ledger sheet will show for itself. We bought stock and loaned money to Producers' Finance Company, but I haven't got the dates clear in my mind.

Q. That was in 1948, Mr. Koch?

(Testimony of Maurice P. Koch.)

A. It was either 1947 or 1948. I think the account 40 will show that, our ledger sheet.

Q. With reference to the money advanced by Producers' Finance Corporation, do you have that check for \$8,000.00 that you referred to yesterday?

A. Yes, sir, I believe we have.

Mr. Gillard: Do you have that check?

Mr. Fink: I showed it to you yesterday.

Mr. Gillard: As defendant's next in order, I will offer the check of Producers' Finance Corporation by Maurice P. Koch, President, dated July 8, 1948, in the sum of \$8,000.00 made payable to Max Fink.

(The document referred to was thereupon received in evidence and marked Defendant's Exhibit I.)

Q. (By Mr. Gillard): I will hand you Exhibit I, Mr. Koch, and also Plaintiffs' Exhibit 34. Is Exhibit I the check that was referred to and mailed to Mr. Fink in connection with Exhibit No. 34?

A. Yes, sir. [159]

Q. Of the total amount of money that was spent for the purchase of "The Hill of the Hawk" and for your stock in Ambassador Pictures Corporation, that was a total of \$25,000.00, is that so, sir?

A. A total of \$25,000.00 was spent for "Hill of the Hawk."

Q. \$17,000.00 of that was your money which went into Ambassador Pictures Corporation and from there was used by that corporation to buy the book, is that so?

(Testimony of Maurice P. Koch.)

A. \$7,000.00 was paid for the stock, and also that \$7,000.00 was used by the corporation for the first down payment of "Hill of the Hawk," and subsequent to that the other \$18,000.00 was loaned to Ambassador Pictures to buy "Hill of the Hawk."

Q. That \$25,000.00 was all subsequently returned, was it, Mr. Koch? A. That is right.

Q. The \$8,000.00 represented by this check, Exhibit I, the last one just shown to you, was returned to Producers' Finance Corporation, is that correct?

A. That is right.

Q. The other \$17,000.00 was repaid to you personally, was it? A. That is right, sir.

Q. And that did not go back to H. Koch & Sons or through its books? A. That is right.

Q. During the period 1946 and 1947 was any picture produced [160] by virtue of any financing activities that you have testified to with the exception of "Copacabana"?

A. 1946 and 1947? No. We worked on a lot of pictures but they were not completed, produced.

Q. Mr. Koch, did you ever make any demand upon Mr. Sebastian for the return of the \$17,500.00 advanced to him?

A. No, sir, there was no need of that.

Q. Did you ever make any demand for its return? A. No, sir. May I explain that?

Mr. Gillard: I think your counsel will take care of that. Thank you, Mr. Koch.

(Testimony of Maurice P. Koch.)

Redirect Examination

By Mr. Fink:

Q. Mr. Koch, I have some questions, too, if you don't mind. You just mentioned that you wanted to explain why you had not made a demand upon Mr. Sebastian for \$17,500.00. Will you explain that to us, Mr. Koch?

A. Yes, sir. That money was advanced, that \$17,000.00 was advanced to Mr. Sebastian. \$10,000.00 of that went to Coslow and Hersh to buy stock in the Beacon Pictures Corporation. If the picture was made and completed and profits were forthcoming, then that money, when the company was dissolved, that money would be forthcoming back to me, plus the interest in the picture, and if the company did not make any money and they did not get any money back, that money would be a loss. I mean, there would be nothing coming back to me. That was [161] understood. The same thing applied with the \$7,500.00 that Sebastian and Hersh received for expenses to get the picture rolling. In other words, this \$17,500.00 was treated exactly the same as the \$80,000.00 that we put into Beacon Pictures Corporation, and that is why we never asked for the money back, because there was nothing forthcoming from the picture.

Q. Mr. Koch, I will run through a few things that you testified about yesterday. Yesterday counsel asked you about gross sales, I believe, of H. Koch & Sons, the copartnership, and showed you Exhibit



(Testimony of Maurice P. Koch.)

C, a partnership return. I think you told him that gross sales in the year 1947, in accordance with that exhibit, were \$555,532.46. What was the net income for the entire partnership that year?

A. The income was \$19,223.18.

Q. That was divided between how many partners?

A. Four partners.

Q. Around \$4,780.00 each?

A. That is right.

Q. For the year?

A. That included our salaries, I believe.

Q. I note here in the year 1946——

The Court: What do you mean, it included your salaries? You mean your salaries were in addition to that, do you not?

A. I don't believe our salaries were in addition to that, [162] Your Honor.

Mr. Fink: It is a partnership.

The Court: I want to know what you mean by "included our salaries."

A. In a partnership our profit includes our salaries. In other words——

Q. I don't want any discussion about it. Did you get any salary in addition to the \$19,000.00; yes or no?

A. No, sir. No, sir.

Q. (By Mr. Fink): I will show you here on Schedule I of the same partnership return, Exhibit C, "H. M. Koch, \$4,805.48."

A. That is part of the salary, that is right.

Q. W. E. Koch, also, \$4,805.00?

A. Yes.

(Testimony of Maurice P. Koch.)

Q. M. P. Koch, also, \$4,805.00? A. Yes.

Q. Rebecca Koch, \$4,805.00?

A. That is right.

Q. Plus the odd cents. I notice in 1946 that your tax return shows a net income of \$115,000.00. Will you tell me, Mr. Koch, was the luggage business that you were in at that time going downhill?

A. The luggage business in 1946 was better than it was in 1947.

Q. In 1947 you made about \$4,805.00 apiece. What happened [163] in 1948?

A. In 1948 it was worse than 1947.

Mr. Gillard: If the Court please, I am going to object to this line of questioning, not because I want to keep it from the jury, but because I do not think it is relevant to the issues in the case. The exhibits, of course, are not limited in purpose. I put them in to show the gross activity of Mr. Koch.

The Court: There is no question before the Court. The answer is in. Proceed.

Q. (By Mr. Fink): Mr. Koch, at the end of 1947 what was the cash position of H. Koch & Sons, a partnership, on December 31, or thereabouts, of 1947?

A. We had practically nothing in the bank. I believe we owed money.

Q. Did you intend during the years 1946 and 1947 to get into and be a part of the motion picture business?

Mr. Gillard: I object to that as incompetent, irrelevant and immaterial.

(Testimony of Maurice P. Koch.)

The Court: I will permit the answer "yes" or "no."

The Witness: Yes.

Q. (By Mr. Fink): What was your reason for that?

A. Well, I was on the War Production Board during the war. I made four or five trips to Washington every year.

The Court: That is going a little far afield, counsel. [164]

The Witness: I want to explain this situation of the business.

The Court: I do not want to hear a long story of things that are not pertinent to this inquiry, please.

Q. (By Mr. Fink): What was your reason for becoming active in this motion picture finance business?

Mr. Gillard: I object to that as incompetent, irrelevant and immaterial.

The Court: I will permit him briefly to give an answer.

The Witness: Well, I had every reason to believe that with the number of manufacturers, the increased number of manufacturers going into the luggage business that the supply was going to overwhelm the demand, and we had to get into something else to make money or we were going to be out of luck.

Q. (By Mr. Fink): Did you eventually go out of the motion picture finance business?

(Testimony of Maurice P. Koch.)

A. Yes, sir.

Q. When?           A. Well, in——

Mr. Gillard: I object to that, if your Honor please, as incompetent, irrelevant and immaterial. The issues here are 1946 and 1947. We haven't engaged in transactions up to the present time.

Mr. Fink: Counsel asked the witness yesterday about [165] selling out to Jack Chertok, your Honor, which happened in 1949, and I thought we should establish just when he discontinued——

The Court: I think it calls for a conclusion and the objection may be sustained.

Q. (By Mr. Fink): Mr. Koch, counsel asked you yesterday about your activities in selling luggage in 1946, and I think you told counsel that you were selling luggage in 12 Western States. How much of your time was devoted to selling in 1946?

A. In 1946 everything was on allocation.

Q. What do you mean by that?

A. Well, luggage was practically impossible to be obtained. The war was over, and we allocated luggage to all our customers. In other words, we gave them a quota and shipped them that quota every month. Never called on hardly anybody.

Q. In 1947 I believe you told counsel you engaged agents to sell on commission?

A. That is right.

Q. Yesterday counsel inquired of you with regard to a law suit, a judgment against Beacon that was filed in the Beacon Pictures Corporation, a

(Testimony of Maurice P. Koch.)

bankruptcy proceeding. He read to you only four lines on page 38 of your deposition. Starting at page 38, line 20, to and including line 24:

“Q. Mr. Koch, this suit was—the basis of this suit was two promissory notes signed by Beacon Pictures [166] Corporation, each in your favor, one for \$50,000.00 and one for \$30,000.00, wasn’t it?

“A. That is correct.”

Now, Mr. Koch, I want to read to you the very next five lines of your deposition:

“Q. And those two notes were the basis of the action filed against Beacon Pictures Corporation, isn’t that right?

“A. Well, I think my attorney can tell you more about that than I can. He filed that suit. I turned the whole thing over to him and walked away, and that is the truth.”

Was that your testimony?

A. Yes, sir.

Q. Did you at any time attempt to direct your attorneys as to what legal theories should be pursued in this situation?

A. No, sir.

Q. By the way, you mentioned that you sold out Ambassador Pictures and “Hill of the Hawk” to Jack Chertok. Do you know whether or not he has ever produced or ever will produce the feature picture called “Hill of the Hawk”?

A. I believe he is working on it right now.

Q. I think you told us that you had your attorney, Mr. Grupp, in San Francisco incorporate Producers’ Finance Corporation?

(Testimony of Maurice P. Koch.)

A. That is right.

Q. And the incorporators of that were yourself, Mr. Grupp [167] and Mr. Grupp's secretary?

A. That is right.

Q. This was done in 1947, wasn't it?

A. 1947, yes, sir.

Q. What was the purpose of forming this corporation?

A. This corporation was formed to finance motion pictures.

Q. What do you mean by financing?

A. To advance the money for the pre-production of motion pictures, with participation in the motion pictures.

Q. Did you intend to obtain outside capital through this corporation? A. Yes, sir.

Q. Did you obtain outside capital through this corporation? A. Yes, sir.

Q. When I say "outside," I mean outside the Koch family.

A. That is right, sir.

Q. Did you ever receive any salary from Producers' Finance Corporation? A. No, sir.

Q. Did you ever receive any salary from Apex Films or Ambassador Productions or Beacon Pictures Corporation or any of the other corporations that have been mentioned in this case?

A. No direct salaries.

Q. And in speaking about your past experience and knowledge [168] of the picture business, among

(Testimony of Maurice P. Koch.)

other things, Mr. Koch, yesterday you mentioned your father-in-law. You did not tell us, I don't believe, what his relationship was to that. Was your father-in-law in the picture business?

A. Yes, sir, he was one of the big producers in his day.

Q. What was his name?

A. Arthur Harry Sebastian.

Q. What was the nature of the business he was in?

A. He was a producer and actually produced many pictures.

Q. So far as other members and relatives in your family are concerned, were other men in the theatre and the theatrical business?

A. Yes, sir.

Q. Were any of them, for example, in the theatre business?

A. Yes, sir.

Q. To what extent?

Mr. Gillard: I will object to that as incompetent, irrelevant and immaterial.

The Court: Sustained.

Q. (By Mr. Fink): In your earlier years, Mr. Koch, did you have the opportunity of learning from members of your family facts concerning the motion picture industry and the motion picture business?

Mr. Gillard: I object to that as calling for the opinion and conclusion of the witness. [169]

The Court: Sustained.

Q. (By Mr. Fink): I think you told counsel

(Testimony of Maurice P. Koch.)  
yesterday that you never made a picture yourself and you do not know anyone who ever has. What did you mean by that?

A. There is no one man who can make a picture. It takes an organization.

Q. Mr. Koch, I think you told us that United Artists Picture Corporation sells pictures worldwide, and that the picture "Copacabana" was entrusted to them for sale throughout the world, is that correct? A. That is right.

Q. After you learned from the sales of "Copacabana," United Artists, that the picture was a total loss so far as your money was concerned in the year 1947, did you file an amended partnership return for the year 1947? A. I believe we did.

Q. I will show you here what is called "Amended Return, United States Partnership Return of Income, 1947." A. Yes.

Q. The caption is, "Amended Return." On the last page appears a signature.

A. That is right.

Q. Is that your signature? A. Yes, sir.

Q. Is this the amended return that you [170] filed? A. It evidently is, yes.

Q. For H. Koch & Sons? A. Yes, sir.

Q. It shows a net loss for the year of \$55,776.82, is that correct? A. That is correct.

Q. For the partnership business.

Mr. Fink: May I offer this as plaintiffs' Exhibit next in order?

Mr. Gillard: If the Court please, this is, I be-



(Testimony of Maurice P. Koch.)

lieve, rendered irrelevant by the pleadings. The answer of the Government admits that a loss of \$75,000.00 was incurred and a claim was made for that by the partnership. There is no issue in the case with respect to this matter.

The Court: The objection is overruled. It may be admitted and marked Exhibit 35.

(The document referred to was thereupon received in evidence and marked Plaintiffs' Exhibit 35.)

Mr. Fink: We have no further questions at this time, your Honor.

Mr. Gillard: No further questions.

The Court: You may step down. Call your next witness, please.

Mr. Fink: We are calling a witness from the witness room, your Honor. Your Honor, when this action was first called on [171] the Master Calendar, Mr. Grupp was permitted to withdraw as counsel in the case due to the fact that he was going to be a witness, and I do not believe that record has come through to your Honor as yet. He is not an attorney in the case at this time.

The Court: Call your witness, Mr. Fink, please.

## MORRIS M. GRUPP

called as a witness on behalf of the plaintiffs, being first duly sworn, testified as follows:

## Direct Examination

By Mr. Fink:

Q. What is your name, please?

A. Morris M. Grupp, 350 Mills Tower, San Francisco.

Q. What is your business?

A. I am an attorney at law.

Q. How long have you practiced in the State of California? A. Since 1927.

Q. Do you know the Koch family?

A. I do.

Q. How long have you known them?

A. I have known the Koch family since approximately 1920.

Q. Thirty-six years? A. That is correct.

Q. Have you been the counsel for H. Koch & Sons, a copartnership?

A. The present partnership, yes. [172]

Q. I show you here Exhibit 1, a copartnership agreement between Rebecca Koch, Maurice P. Koch, Harold M. Koch, and William L. Koch, and ask you if you drafted that document.

A. Yes, sir, I drafted that document.

Q. I will show you an amendment which purports to be executed on the 23rd of October, 1944, by those same people, amending the partnership agreement, originally this Exhibit 1. Did you draft this agreement? A. I did.

(Testimony of Morris M. Grupp.)

Q. Do you recall the circumstances leading up to the amending of the partnership agreement?

A. Yes, to some extent, I imagine.

Q. What were those circumstances insofar as leading up to this amendment, pursuant to which this amendment was prepared? I will withdraw the question. What occasioned the drafting of this amendment to the original agreement?

The Court: I take it that that is a conclusion. The agreement was signed. There is no question about it. It is a completed fact. How can this witness testify to conclusions as to reasons why it should be done?

Mr. Fink: I suppose it will speak for itself, your Honor.

Q. Mr. Grupp, after the 23rd day of October, 1944, did you have any dealings with the Koch family with regard to the motion picture finance business? A. Yes. [173]

Q. I will show you here an agreement of partnership which bears date of the 23rd day of October, 1944, and which bears a number of signatures, including one that purports to be your signature. This is your signature, is it?

A. That is correct, that is my signature.

Q. Did you prepare this agreement?

A. I prepared that agreement.

Q. Did you act under this agreement?

A. I did.

Q. Mr. Grupp, we are concerned here with certain transactions that led into the year 1947. Do you

(Testimony of Morris M. Grupp.)  
recall transactions involving H. Koch & Sons and Beacon Pictures Corporation and a picture, "Copacabana"?

A. Yes, that was one of the later—not one of the later ones, but that was some time after the original transaction that was set forth in the exhibit that you just showed to me.

Q. In between the date of October 23, 1944, and the time that this Beacon Pictures Corporation—"Copacabana" matter came up, there were other considerations, were there not, which you investigated? A. That is correct.

Q. Turning to this matter of Beacon Pictures Corporation and a picture called "Capacabana," do you recall whether or not you were consulted in connection with that matter?

A. Yes, I was consulted by the Koch family. I had various [174] conferences.

Q. Approximately when were you first consulted and did you first confer with regard to that matter?

A. As to the date, I would say approximately the middle of 1946 or somewhere along in there.

Q. Let us put it this way: Do you know whether or not a picture called "Copacabana" was made?

A. Yes.

Q. You saw the picture?

A. Yes, I did. I saw it being made.

Q. Were your conferences and consultations prior to the making of that film?

A. I would say about six months before that,

(Testimony of Morris M. Grupp.)

or four months, five months, somewhere along in there.

Q. In any event, we are talking about a situation that occurred approximately ten years ago?

A. Yes.

Q. We do not expect you to be exactly accurate on it. At that time whom did you represent?

A. I represented the copartners in the Koch enterprise and the Koch family.

Q. That was then H. Koch & Sons?

A. That is correct.

Q. The copartnership with which we are concerned here? A. That is right. [175]

Q. Did you meet a man named David Hersh?

A. Yes, Mr. Hersh came to San Francisco when I originally met him in my office. We had an evening conference, as I recall it, which lasted all evening.

Q. Did you discuss the matter of this proposed arrangement with Mr. Hersh at that time?

A. That is right. That was the purpose of his visit here.

Q. Did you perform that activity as counsel for H. Koch & Sons? A. Yes.

Q. Did you talk to one David Sebastian at or about the same time?

A. Yes, I think David Sebastian brought Mr. Hersh to San Francisco. I know they came together. In the conference that we had, both Mr. Hersh and Mr. Sebastian were present, I think Mr. Maurice Koch was present. I do not recall any of the other Koch family at that meeting.

(Testimony of Morris M. Grupp.)

Q. Do you remember that H. Koch & Sons put some money up for an interest in the film "Copacabana"? A. Yes.

Q. Prior to the time this money was advanced, did you discuss matters relative to that transaction with members of the family or partnership other than Maurice Koch?

A. Yes—well, all the members of the partnership, as I recall it, were at one time or another in one or two conferences [176] together.

Q. Following that time, Mr. Grupp, did you have occasion to be consulted in connection with other motion picture transactions by H. Koch & Sons?

A. Yes, there were quite a number of them.

Q. I will call your attention particularly to the formation of a company called Producers' Finance Corporation.

A. Yes, that was a corporation as distinguished from the Producers' Syndicate. I think the original was Producers' Syndicate. If that is the corporation that was organized, then that is the one I think I organized.

Q. I will show you here Exhibit 25, which purports to be a certified copy of Articles of Incorporation of the Producers' Finance Corporation.

A. Yes.

Q. It purports to have been filed in the office of the Secretary of State on the 20th day of October, 1947? A. That is right.

Q. I will show you the names of the incorpora-

(Testimony of Morris M. Grupp.)

tors, which appear to be Morris Grupp, Maurice P. Koch, and Bernice E. Phillips.

A. That is right. Bernice E. Phillips was my secretary at the time.

Q. Did you and your secretary named here at all times act on behalf of H. Koch & Sons in organizing this corporation? [177]

A. That is right.

Q. At the time that this corporation was organized, I take it it did not have capital at that time, is that correct?

A. At the time it was organized? No, excepting that the Kochs advanced and paid all the costs of the incorporation.

The Court: By incorporation you mean the filing of the Articles in Sacramento?

A. The filing of the Articles in Sacramento and the subsequent applications that were filed for the issuance of stock.

Q. (By Mr. Fink): Did you obtain a permit to issue stock in that company from the Department of Investments of the State of California?

A. I did.

Q. When did you obtain such a permit?

A. The permit was issued on February 26, 1948.

Q. The corporation we noted was incorporated on October 20, 1947.

A. Yes. Then an application follows, as a rule, which it takes some time to act on.

Q. In the several months that intervened between the incorporation of the company and the

(Testimony of Morris M. Grupp.)

obtaining of the stock permit, were any persons, firms or corporations to your knowledge interested in Producers' Finance Corporation other than H. Koch & Sons?

A. Not during that interval of time. During that interval [178] of time it was entirely their corporation.

The Court: So that the jury may understand, Mr. Grupp, what organizing a corporation means, that is done by an attorney preparing a paper which is called the Articles of Incorporation. The parties or the people in your office sign it, and it is mailed to Sacramento.

The Witness: That is correct.

The Court: That is called forming a corporation.

The Witness: That is the forming of the actual corporation.

The Court: Thereafter, if there is any money to be invested, an application must be made to the Corporation Commissioner, and he thereafter issues a permit that the stock may be issued upon certain conditions.

The Witness: That is right, and then if I might follow it from there, as a rule when the corporation gets into action or becomes activated, as a rule the incorporators, if their attorney is secretary, he will step out of the picture and the new directors are voted in and they proceed with their business.

The Court: Until the permit to issue stock is made and the stock is issued, all that is done is the filing of the Articles of Incorporation.



(Testimony of Morris M. Grupp.)

The Witness: That is correct.

Mr. Fink: May I offer this stock permit of Producers' [179] Finance Corporation as plaintiffs' next in order, your Honor?

The Court: Exhibit 36.

(The document referred to was thereupon received in evidence and marked Plaintiffs' Exhibit 36.)

Q. (By Mr. Fink): Mr. Grupp, do you know a Mr. Jack Chertok? A. Yes.

Q. When did you meet him?

A. I would imagine it was either in August or September of 1947. It preceded the date of the organization of Producers' Finance.

Q. Did you meet him in a professional capacity, that is, in pursuit of your profession as an attorney?

A. Yes.

Q. For whom were you acting at the time?

A. For the Koch family and partnership.

Q. Did you have occasion to discuss financial matters pertaining to the picture business with him?

A. I did.

Q. Where did you meet him, by the way?

A. I met him at his office in Los Angeles.

Q. Did you go there to see him?

A. Yes, that was the only purpose of that trip.

Q. Did you have more than one conversation with Mr. Chertok?

A. I cannot be certain whether the second conversation I had in San Francisco was with Mr.

(Testimony of Morris M. Grupp.)

Chertok or one of the members [180] of his staff with reference to a loan that was made with Pacific National Bank. I tried to recollect that, Mr. Fink. I am not certain Mr. Chertok came to San Francisco at that time. My memory was—my best memory would be that he did, and that I met him twice, and that I met another member of his staff once in San Francisco. Once I know I met Mr. Chertok in Los Angeles.

Q. Did you have any financial dealings with Mr. Chertok on behalf of H. Koch & Sons?

A. Yes.

Q. What was the nature of those dealings?

A. Well, it started with this conversation in Los Angeles, where Mr. Chertok explained to me that there was a vital need in the motion picture business of what they called funds, pre-production funds, which he explained were the funds which were necessary to gather a picture to the point where the camera starts to turn, and that that was the most difficult money to obtain, particularly in instances where there were no big stars, big names connected with the picture, and that there was a crying need for any organization that could supply that type of funds, and that he was in that position and would like to get some pre-production money. He gave us his background. I remember he had been with one of the picture studios—I do not know whether it was MGM or one of them—for many, many years, and he himself would be vitally interested in such a [181] group, if such a group were

(Testimony of Morris M. Grupp.)

put together, in joining that group, even to the extent of putting in a certain percentage of his own profits in such an organization upon which he or other producers could later draw.

Then subsequently there were some arrangements made through the bank which the Kochs banked at, the Pacific National Bank, and conferences held there with reference to backing some pictures or financing some pictures which I think Mr. Chertok was making for one of the Departments of the United States Government. I don't remember whether it was the Army or the Navy. But arrangements on that were made in 1947, as I remember it, and then it was quite awhile—I mean, the bank had to commit themselves before Chertok could go ahead and bind himself to the contracts with the Government, which I understand was ultimately done and carried through. Then there were moneys advanced to Mr. Chertok by the corporation at a later date.

Q. Do you know whether or not the Signal Corps and Army and Air Corps training films were produced?      A. Yes.

Q. Some time prior to the production of those films I assume arrangements were made with the Government for the production of them?

A. Yes.

Q. As I think you told us, your arrangements for financing [182] and banking, so far as the production of those films were concerned, were made prior to that time?

(Testimony of Morris M. Grupp.)

A. Yes. The bank—first, there was quite a lot of money involved there, as I remember it, and the bank was vitally interested in the background of Mr. Chertok. They discussed the matter, Mr. Lee Master, I think it was, of the bank, with Mr. Koch on several occasions. I was with them on one or two occasions; I gave him the answer to some of the questions as I understood them, when I had conferences with Mr. Chertok and then the bank, as I recall, finally committed themselves to this financing after this investigation. Then he completed his contracts with the Government.

Q. Could you define this a little more closely, just when these discussions with Mr. Chertok were had and also approximately when it was that the bank as well as the Koch family and the corporation committed the financing necessary to make these films?

Mr. Gillard: I object to that as compound and complex, if the Court please.

Mr. Fink: I merely wanted the time set.

The Court: Does the witness understand the question?

The Witness: I think I understand the question. As I recall, the conference with Mr. Chertok preceded the filing of the corporation papers in Producers' Finance, and Producers' Finance Corporation was organized as a means of carrying into [183] practice such arrangement as could be made with Mr. Chertok.

Q. (By Mr. Fink): I want to call your atten-

(Testimony of Morris M. Grupp.)

tion to the fact that Exhibit 25, the Articles of Incorporation of Producers' Finance Corporation, indicates that they were filed with the office of the Secretary of State of California October 20, 1947.

A. I would say my memory would be it would be between 60 days and 90 days before that.

Q. In any event, these arrangements for financing with the bank, as well as with the Koch family, were made some time, you say, prior to this October 20, 1947, date?

A. Yes. In other words, the first conference with Chertok in Los Angeles, I would say, preceded that by 60 or 90 days. Then after that the question of the Signal Corps pictures, which I now recall that you mention it, came into the discussion.

Q. Did these discussions occur in the year 1947?

A. Yes.

Q. Were these financial commitments made with regard to financing these training films made in 1947?

A. My memory is the bank concluded—I think it took about 90 days or something like that, or more—90 to 120 days to consummate the contracts with the Government after the bank had committed themselves to the financing.

Q. Prior to October 23, 1944, what had been the business of H. Koch & Sons? What business were they in? [184]

Mr. Gillard: I object to that as calling for the opinion and conclusion of the witness.

The Court: I think I will permit him to answer.

(Testimony of Morris M. Grupp.)

The Witness: H. Koch & Sons were manufacturing luggage of various types prior to 1944 and as long as I remember them, the family.

Q. (By Mr. Fink): After the amendment, after October 23, 1944, what was the business of H. Koch & Sons?

The Court: I think that calls for a conclusion. I think this witness is not able to testify to that.

Q. (By Mr. Fink): Were all of the activities which you devoted to this motion picture financing, the time that you spent professionally, was all of this time and all this activity conducted by you as counsel for H. Koch & Sons?

A. Yes, at all times. I do not think that any of the costs, any of the costs that were expended there were advanced by either of the corporations or by any other person other than the Kochs.

Mr. Fink: No further questions.

The Court: We will take a recess at this time.

(Recess.)

Mr. Fink: During the recess my attention was called to an oversight. May I reopen?

The Court: All right.

Q. (By Mr. Fink): Mr. Grupp, during the year 1947, the year [185] in question, were you in touch with Mr. Maurice P. Koch in the course of that year? A. Yes.

Q. To what extent? Will you describe your contact with him? A. During the year 1947—

Mr. Gillard: I will object to the question as

(Testimony of Morris M. Grupp.)

being too broad and general, and not being limited to the activities in connection with the issues in this case.

Mr. Fink: I will withdraw the question and reframe it.

Q. Mr. Grupp, during the year 1947, did you have occasion to discuss motion picture matters with Mr. Maurice P. Koch? A. Yes.

Q. Did you also during that year have occasion to discuss motion picture affairs with other members of the partnership of H. Koch & Sons?

A. Yes.

Q. Insofar as your discussions with Maurice P. Koch are concerned on motion picture matters, on approximately how many occasions during the year 1947, did you discuss such matters with him?

A. I would venture to say fully a hundred times between personal, telephone calls and conferences.

Q. Were those telephone calls local calls or long distance calls?

A. Many of the phone calls—I would venture to say half of [186] them—were from Los Angeles.

Q. Did these 100 times or so during that one single year, the calls and discussions you had, relate to the motion picture business?

A. Entirely to the motion picture business.

Q. Was it a rather constant activity or were there gaps in between?

A. It was almost constant, every two or three days, sometimes day after day, sometimes several times a day. It was a constant activity on that dur-

(Testimony of Morris M. Grupp.)

ing practically the whole year, as I recall, one thing or another.

Mr. Fink: That is all.

### Cross-Examination

By Mr. Gillard:

Q. Mr. Grupp, do you have a day book showing your contacts with Mr. Koch?

A. I do not know whether I have a day book from that time past. If I do, it would be in the storage of the basement of the 417 Market Street building, where I have stored old records. I would venture to say, Mr. Gillard, that the day book would not show numerous phone calls which I received at my home, 12:00 o'clock midnight, 2:00 o'clock in the morning, at any time almost during a good portion of that year.

Q. Mr. Grupp, I gather the day book would show the conferences in your office that you had.

A. If conferences were scheduled, it would show that. [187]

Q. You did not consult that day book, I take it, prior to your testimony today?

A. No, I did not.

Q. When was the first time that you went to the bank with Mr. Koch with reference to the financing for Apex Films?

A. I would venture to say it was within 30 days or 60 days before that corporation, Producers' Finance, was formed. I think it was formed some time in the later part of October. It followed within



(Testimony of Morris M. Grupp.)

several weeks at least of my first visit to Mr. Chertok in Los Angeles.

Q. Do you know of your own knowledge that the bank advanced money in that connection to Apex Film Corporation?

A. Yes. You mention Apex. I think that was the name.

Q. The money was not advanced to Producers' Finance, was it?

A. No, it was advanced to whatever company Mr. Chertok was operating under at that time.

Q. Do you know when money was advanced by the bank?

A. No, I do not know when it was, as my memory serves me now. I mentioned before, after the bank committed itself to make these loans, Mr. Chertok proceeded to complete his contractual arrangements with the Signal Corps, I would imagine some 60, 90 or 120 days intervened. I would imagine they must have gotten the money early in 1948.

Q. Did the bank require that the Apex Corporation have on hand the pre-production money prior to its loan? [188]

A. I do not recall that. I didn't handle the bank papers for the Apex Company and I do not know what their requirements precedent to their making the loan was. There was some moneys I know that came to Apex from Producers' Finance, but just what that pertained to at that time I do not recall.

Q. Mr. Grupp, after all of your experience in the motion picture financing business, acting as the

(Testimony of Morris M. Grupp.)

attorney for the Koch family, wasn't it your experience that the primary financing money from banks was not put up until there was available and on hand the pre-production money?

A. That was so. Now, you say "with all my experience." I, unfortunately, had very little experience prior to this with reference to motion picture financing, and my experience came as a result of my conferences first with Mr. Hersh, who educated me along those lines, and then with Mr. Chertok, and then through Mr. Koch, who had some dealings down there with the bank and one of the finance companies in Los Angeles, about which he discussed with me.

Q. I will show you Exhibit H. Exhibit H, Mr. Grupp, is the letter from Producers' Finance Corporation signed by M. P. Koch and directed to Mr. Jack Chertok, in which he is discussing in a preliminary way their negotiations for the lending of money from Producers' Finance to Apex. You will notice by virtue of the terms of that document that no money has yet been advanced to Apex. Under those circumstances, and keeping [189] in mind that date of January 29, 1948, is your memory refreshed as to when money was advanced by Pacific National Bank to Apex?

A. No, this could not refresh my recollection. With reference to that transaction, Mr. Gillard, I tried to explain the bank's position was that they were relying upon Mr. Koch's investigation of this matter and the knowledge of Mr. Chertok and his

(Testimony of Morris M. Grupp.)

background. Before they were even considering the matter, they wanted to know from him primarily what that background was, and they were also inexperienced in the motion picture field.

Q. Would you mind trying to answer my question, Mr. Grupp?      A. What is your question?

Q. My question was, does this refresh your recollection as to the date the bank advanced the money to Apex Films?      A. No.

Q. Were you the legal counsel for Producers' Finance Corporation?      A. Yes, sir.

Q. You were?      A. Yes, sir.

Q. And from the date of its incorporation you were acting as legal counsel for Producers Finance Corporation?

A. When I say "legal counsel," I was here in San Francisco; Mr. Fink was in Los Angeles, and he may have acted when Mr. [190] Koch was down there with the same authority that I had here.

Q. I am talking about Producers Finance Corporation.      A. Yes.

Q. You were the attorney for that corporation?

A. Yes.

Q. From the date of its incorporation on in connection with these affairs, you acted as counsel for Producers' Finance Corporation?      A. Yes.

Mr. Gillard: Thank you, Mr. Grupp.

Mr. Fink: We have no questions.

The Court: Just a moment, Mr. Grupp. I wanted to ask you a question.

Q. In these conferences and advice that you had

(Testimony of Morris M. Grupp.)

during the year 1947 with Mr. Koch and with the persons whom you have mentioned, were you acting in your professional capacity as an attorney for H. Koch & Sons?      A. Yes.

Q. Calling your attention to the exhibit in this case, Exhibit C, which is the 1947 income tax return of H. Koch & Sons under the heading of "Expenses, legal and auditing," \$268.00, is that the amount of fee that you charged for your services during that year?

A. I did not charge one cent for services, your Honor, to the Koch family from 1932 until about three years ago—not [191] one cent was ever paid me as attorney's fees by the Koch family.

Q. Then you did not receive any part of that \$268.00 in 1947?

A. It may have been costs, actual costs, or a portion of that may be actual costs I had advanced or that the Koch family paid me for filing fees, for documentation, and so forth, but as far as fees were concerned, there were no fees paid.

Mr. Fink: May I ask a question?

The Court: You may.

#### Redirect Examination

By Mr. Fink:

Q. How did it happen, Mr. Grupp, that you did not charge a fee for your legal services to the Koch family over those years in which you have described the numerous activities, particularly 1947?

A. I should figure it dates back to 1932, at a

(Testimony of Morris M. Grupp.)

time when I was very young in my practice. The Koch family, Mr. Koch was a very close friend of mine, my family's, and during the years of 1931 and 1932 Mrs. Grupp was quite ill, and during that time, and during a period of some 12 to 15 weeks that she was in the hospital, Mr. Koch advanced—I had on my desk a check every week for the time she was in the hospital for all the doctors', hospital bills, nurses' bills, which amounted to something over \$12,000.00, which was thereafter repaid to him by bank loan. This was all voluntary on his part, and when [192] she got out of the hospital, he presented me with a 1930 Buick automobile, which he took back from one of his salesmen, and after that, very frankly, until long after his death, and until more recently when their plant was flourishing, and upon the insistence of the Kochs, I never rendered a bill for legal services to the family or any member of the family for anything I had done for them. I just could not do it.

Q. You say "after his death." You mean the father?

A. That is correct.

(Witness excused.)

**MARTIN EISENBERG**

called as a witness on behalf of the plaintiffs, and being first duly sworn, testified as follows:

The Court: Will you state your name?

The Witness: My name is Martin Eisenberg.

**Direct Examination**

By Mr. Fink:

Q. Mr. Eisenberg, where do you live?

A. I live at 510 South Burnside Avenue, Los Angeles, California.

Q. What is your business or occupation?

A. I am a financial and production supervisor in the motion picture industry.

Q. Did you have any training for that particular calling? A. Yes, I do. [193]

Q. What was your training?

A. My training was the coast—costing of—by reason of an accounting background——

Q. You were an accountant at one time, were you? A. Yes, I was.

Q. That was many years ago?

A. Many years ago.

Q. Did you go into cost accounting work?

A. Yes, I did.

Q. In connection with the motion picture business, how long have you been identified with that industry? A. Since the fall of 1932.

Q. Some 24 years ago? A. 24 years ago.

Q. Has all your activity in that business been principally in Hollywood?

(Testimony of Martin Eisenberg.)

A. Principally in Hollywood.

Q. And has it been principally in connection with the production of films?

A. Always the production of motion picture films.

Q. Calling your attention to the year 1946, do you recall the making of a picture called "Copa-cabana"?

A. Yes, sir.

Q. Prior to the actual principal photography of that picture, had you had any relationships with Bank of America? [194]

A. Yes, I had.

Q. What was the nature of that relationship?

A. I had served as controller by appointment and being approved by the Bank of America and other banks to serve in the capacity of controller of the motion picture producing companies.

Q. And have you followed that same type of activity over these years?

A. All during this period.

Q. By the way, you work, I take it, primarily in the so-called independent field?

A. Wholly.

Q. Can you describe for us what we generally refer to as independent productions, how they differ from so-called major studio productions?

A. An independent producing organization is formed by certain individuals for the purpose of producing one or more motion picture features or so-called B pictures for distribution through independent motion picture distribution agencies. That

(Testimony of Martin Eisenberg.)

is distinctive of the distribution as afforded by the major studios' own distribution setups.

Q. In the years 1946 and 1947 were you acquainted with an organization called the United Artists Corporation? A. Yes, I was.

Q. Did you have a constant course of dealings with that [195] organization during that period of time? A. I had, since 1932.

Q. Was United Artists Corporation a so-called distributor for so-called independents?

A. They were wholly.

Q. Did United Artists Corporation make their own pictures? A. No, sir.

Q. They distributed only independent films?

A. Only independent product.

Q. Did you have an acquaintanceship with a Mr. George Backnell? A. Very intimately.

Q. What was his business in 1946?

A. He was vice president in charge of the independent motion picture production on the West Coast.

Q. Were you in touch with him during the year 1946 and the years prior thereto and thereafter?

A. Almost daily.

Q. I will show you here Plaintiffs' Exhibit 5, which I believe is only in for identification up to this point, and ask you if you recognize the signature.

A. The top signature is George Backnell, vice president, and the second signature is Sam Coslow,



(Testimony of Martin Eisenberg.)

who is a producer of Beacon Pictures Corporation, "Copacabana."

Mr. Fink: Your Honor, I may be in error on this. I do [196] not know whether 5 is in evidence or just for identification so far.

The Court: It is only for identification.

Mr. Fink: May I offer it at this time?

Mr. Gillard: I do not think it has any bearing upon any of the issues in this case, if the Court please, a contract executed by parties that are independent to this transaction. For that reason I will object to it.

The Court: Can you show me a connection here, counsel?

Mr. Fink: I thought so, your Honor, but I will continue on with the witness, if I may, to have the record clear in that regard.

Q. Mr. Eisenberg, I will show you Exhibit 5 for identification, which purports to be the agreement between Sam Coslow and United Artists Corporation, and I will ask you if this is not the agreement under which the motion picture "Copacabana" was distributed. A. It is.

Mr. Fink: May we offer it again, your Honor?

The Court: Counsel, what is the connection of that with the parties to this litigation? It has been testified the picture "Copacabana" was made. How does this contract assist in any way in showing these issues?

Mr. Fink: It is part of the over-all picture, to show the contribution of each person toward the

(Testimony of Martin Eisenberg.)  
entire pot that makes [197] an independent picture. This man contributed a release, somebody else contributed something else, and I think we might have it all brought to the attention of the Court.

The Court: At the moment I will sustain the objection. I will look at the document, however.

Mr. Fink: Shall I proceed, your Honor?

The Court: Surely.

Q. (By Mr. Fink): Mr. Eisenberg, did the Bank of America make a loan with regard to the picture "Copacabana"? A. Yes, they did.

Q. Do you recall approximately when the first funds from the Bank of America in connection with that loan were made available?

A. The first funds were toward the end of November or the early part of December. I do not recall exactly the week, but it was just one week apart, either the last week of November or the first week of December.

Q. 1946? A. 1946.

Q. Just prior to the release of those Bank of America funds, just prior to the release of that money, did you appear at the studio in connection with this film? A. Yes, I did.

Q. Did you remain there during the production and filming and the cutting of this picture? [198]

A. I did.

Q. Insofar as the relationship with the bank is concerned, the Bank of America, what was the nature of your duties?

A. I was the approved controller by the bank,

(Testimony of Martin Eisenberg.)

to be employed by Beacon Pictures Corporation, to see to it that the moneys contributed by the various money lenders would be properly disbursed in accordance with the provisions of the budget and the contractual obligations on which that budget was based.

Q. Approximately how long prior to the advance of the first bank money was it that you appeared on the scene of this picture?

A. I believe I came in there around November 18, 1946.

Q. Had this picture been in preparation for some time prior to November 18, 1946?

A. I understood that the picture had been in preparation beginning with April of 1946.

Mr. Gillard: I move that the answer go out as being obviously a hearsay statement.

The Witness: No, it was not a hearsay statement, sir. It was knowledge I acquired after I came on the scene and they were all part of the record.

The Court: I will permit it to remain. Let me ask you one question, counsel.

Do you contend that in Exhibit 5, which consists of something over 40 pages, that there is any reference to H. [199] Koch & Sons or to Maurice P. Koch, or to the obligations or duties that they had in connection with this?

Mr. Fink: No, your Honor.

The Court: Then the objection may be sustained.

(Testimony of Martin Eisenberg.)

Mr. Fink: Do you care to hear from counsel on the matter?

The Court: No, I just wanted to know if there was any connection. I looked through it. I could find no such reference, and if there is no such reference the objection may be sustained.

Q. (By Mr. Fink): Were facilities rented for the making of the picture "Copacabana"?

A. They were.

Q. Who were they rented from?

A. Goldwyn Studios.

Q. When you came to the studio after the months of preparation, and just prior to the advancement of the bank loans, did you meet Mr. Koch? A. Yes, I did.

Q. Maurice P. Koch, here in the courtroom?

A. The gentleman sitting right in front of me.

Q. Had you ever met him prior to that time?

A. No, sir.

Q. Did you meet him on the first day of your arrival? A. I did, sir.

Q. Did you see him thereafter? [200]

A. Time and again.

Q. During the course of the production?

A. Pre-production and during the production of the motion picture.

Q. During that period of time did you observe his activities?

A. Yes, I had occasion to observe them.

Q. What were his activities insofar as the picture "Copacabana" are concerned?

(Testimony of Martin Eisenberg.)

A. Well, his activities were in connection with having furnished the pre-production moneys, and guiding through some financial difficulties that had occurred which deferred the original starting date of the production, which had been some time in the early part of November, to the latter part of November, 1946.

Q. I take it difficulties of various types are not unusual in the motion picture business?

A. No, they are not. They are rather common.

Q. Was Mr. Koch at this studio and active in connection with this film for the period of time after you started your activities there?

A. Yes.

Mr. Gillard: I object to that as ambiguous.

The Court: You can ask him whether he was at the studio, and then go into what he was doing, if you want to.

Q. (By Mr. Fink): What did Mr. Koch do from the time he [201] first came there and you met him?

A. During that time and possibly for ten days thereafter Mr. Koch was engaged with the various contributors to the motion picture production in straightening out not alone the financial difficulties but in lending a hand and guiding the production about to be produced, the elements of some of the production activities.

Q. Could you give us an example in that respect?

A. Yes. There was—Mr. Koch, I recall, sug-

(Testimony of Martin Eisenberg.)

gested that there was altogether too many dance numbers to go into the filming or the production filming that might be unnecessary because of the length of the finished picture; that would be overproduction. Then there were questions of wardrobing and many others of that nature which he helped to balance out with the rest of the interested parties in the production activities.

Q. Did these matters that he assisted in have relationship to the over-all cost and expenditures in the picture making?

A. They certainly had, because if they had not acted on his suggestions, the picture would have gone way, way over the budgetary cost.

Q. You say you met him the first day you came there and you saw him for approximately ten days thereafter. Now, after that time was he gone for awhile? A. Yes, he was. [202]

Q. Did you see him from time to time again after he left? A. Yes, I did.

Q. Were his activities of a similar nature throughout the filming of that picture?

A. The most difficult part was the time when I first met him after the production started, and they acted on his suggestions, and the production ran more or less smoothly.

Q. Who were the owners of this film "Copacabana"?

A. Well, the owner of the film was the Beacon Pictures Corporation.

(Testimony of Martin Eisenberg.)

Q. Did Mr. Koch have any interest in the film-ing?      A. Yes, he did.

Q. Who were the stars of the film?

A. The stars of the film were Grouch Marx——

Q. May I stop you there? Did Groucho Marx own part of the film?      A. Yes, he did.

Mr. Gillard: If your Honor please, I move to strike the last answer so I may make an objection to it, and then I object to the question on the ground it calls for the opinion and conclusion of the witness.

The Court: The answer may go out. Presently I think it does call for his conclusion.

Q. (By Mr. Fink): Do you know whether or not this film was owned by more than one [203] person?

Mr. Gillard: I object to that as calling for an opinion and conclusion of the witness.

The Court: If there is any document which shows the ownership of this film, and there is any question about it, I think the document would be the best evidence.

The Witness: I did——

The Court: Just a moment.

Mr. Fink: Your Honor, we have the document in evidence with regard to the Koch situation, but we certainly do not have the documents with regard to the other people, and I would like to go into somewhat the division of the ownership.

The Court: We are only interested here, counsel, with the activities of H. Koch & Sons, if any.

(Testimony of Martin Eisenberg.)

If you intend to prove any other ownership, I judge you should do it in the legal way, by such documents that there may be, if there are any.

Mr. Fink: Perhaps we can reach it in a different way, your Honor.

Q. Mr. Eisenberg, with how many feature motion pictures have you been associated over your years of experience?

A. Well, about 40 features, about 50 B's, and 330 one-half hour television shows.

Q. Have your activities in the so-called independent motion picture making been continuous throughout the years you have told us about? [204]

A. Yes, they have.

Q. Are you familiar with the term "packaging" in independent films? A. I am.

Q. What does that term generally mean?

A. The packaging is the contribution by the various persons or organizations all brought together for the purpose of producing one or more individual motion pictures.

Q. Are you familiar with the packaging that went to make up the picture "Copacabana"?

A. Yes, I am.

Q. What was that package?

The Court: Was there a written document evidencing that?

The Witness: Yes, there was.

The Court: I take it the written document is the best evidence of what the package was, counsel.

Mr. Fink: No further questions, your Honor.



(Testimony of Martin Eisenberg.)

Cross-Examination

By Mr. Gillard:

Q. Mr. Eisenberg, I am not quite certain by whom you were employed in connection with "Copacabana."

A. There is a custom in the industry——

Q. No, by whom were you employed?

A. I was employed by Beacon Pictures, Inc.

Q. Was it your function to be the controller of the production? [205]           A. It was.

Q. It was your function to examine the budget of the picture and determine that its budget costs were within the amount of money available to be spent?

A. No, that is not the duty of the controller.

Q. What are the duties of the controller?

A. A motion picture controller is one who has the knowledge and experience of the costs of the elements of motion picture production and their administration.

Q. I gather that you testified you were employed as controller on the approval of the Bank of America.

A. That is correct. That is the custom in the industry, because the bank has to have some responsible person upon whom they can depend, that the moneys loaned by the bank and other financial interests contributed by others along with the bank are disbursed properly.

(Testimony of Martin Eisenberg.)

Q. In determining whether or not those funds are disbursed properly, was it not part of your duty to determine that no more funds were expended than were available for the production?

A. That can't always be the case, because sometimes we have difficulties in the course of the production that require additional money to be expended, and that is what they call a picture going over a budget, or costing more than they anticipated it to cost.

Q. Was the budget, as originally set up for "Copacabana," in [206] excess of the amount of money available through the first and second—

A. No, it was less.

Q. It was less. You referred to certain activities on the part of Mr. Koch in making suggestions with reference to eliminating some dance routines, is that correct?

A. Not alone that.

Q. Let us take them one at a time.

A. O.K.

Q. Did he have any authority to cut out those dance routines?

A. No, he as an individual did not have, but by collaboration and discussion, they arrived at the concerted opinion of all those who attended the production meetings, and a lot of his suggestions were followed and saved a lot of money.

Q. I believe you testified his function in being there was as the man who had put up the pre-production money.

A. Yes.

(Testimony of Martin Eisenberg.)

Q. And his purpose in being there was to try to protect his investment so far as he could?

A. That is correct.

Mr. Gillard: That is all.

Redirect Examination

By Mr. Fink:

Q. How many other owners were there of the film "Copacabana"?

Mr. Gillard: I will object to that as calling for the [207] opinion and conclusion of the witness and not being the best evidence.

The Witness: That would not be so, sir, because I do happen——

The Court: Mr. Eisenberg, when an objection is made, the Court will rule as to whether you can answer or not, if you will just wait a moment, please.

The Witness: I beg your pardon.

The Court: Do you expect to pursue that question further, counsel, if he answers it "yes" or "no"?

Mr. Fink: Yes, your Honor. If he answers the question, I expect to pursue it further.

The Court: I will permit the answer as to a number for the purpose of getting that fact. The question is, how many owners were there? I will overrule the objection that far, because there is no question about it. There were some different inter-

(Testimony of Martin Eisenberg.)  
ests in it. Answer that. How many owners were there?

The Witness: There were more than six or seven.

Q. (By Mr. Fink): Was Mr. Koch one of those owners?

Mr. Gillard: I object to that as calling for the opinion and conclusion of the witness, your Honor.

The Court: I think it does call for an opinion. If there is anything that shows his ownership, counsel, and it is in evidence, then why ask this witness about it? [208] Is it in evidence?

Mr. Fink: Exhibits 16 and 17, your Honor.

The Court: All right.

Mr. Fink: Those are the written documentation on it.

The Court: Why go into it further with this witness?

Mr. Fink: Except certain new phases were opened up on cross-examination.

The Court: Ask your next question.

Q. (By Mr. Fink): Counsel asked you for a conclusion as to under what guise Mr. Koch was acting at the time he was at the studio. Did he act as one of the owners of this film? A. Yes——

Mr. Gillard: I object to that as calling for the opinion and conclusion of the witness.

The Court: That is sustained.

Mr. Fink: No further questions, your Honor.

Mr. Gillard: No further questions.

The Court: May I see counsel at the bench?

(Discussion between counsel and the Court at the bench out of the hearing of the reporter.)

The Court: We will take a recess at this time until 1:45, not 2:00 o'clock this afternoon, but [209] 1:45.

Wednesday, November 28, 1956—1:45 P.M.

Mr. Fink: Call Mr. Sebastian.

The Court: There was a witness on the stand, was there not? Had you finished with the witness entirely?

Mr. Fink: I thought we had, your Honor.

Mr. Gillard: Yes.

DAVID A. SEBASTIAN

called as a witness on behalf of the plaintiffs, being first duly sworn, testified as follows:

Direct Examination

By Mr. Fink:

Q. State your name, please.

A. David A. Sebastian.

Q. Mr. Sebastian, where do you live?

A. I live in Beverly Hills, California.

Q. What address?

A. 127 North Swall Drive.

Q. What is your occupation, Mr. Sebastian?

A. I am an assistant producer. I have been a film editor prior to that.

Q. That is in the motion picture industry, is it?

A. Yes.

(Testimony of David A. Sebastian.)

Q. How long have you been connected with the motion picture industry?

A. Approximately 27 years. [210]

Q. Most of your adult life?

A. Most of my adult life.

Q. Prior to your coming into the motion picture business personally, were members of your family connected with that business?

A. Yes, my father was a producer.

Q. Were other relatives in either picture production or exhibition business?

A. Yes, my brother was also a producer and was also in the theatre business.

Q. To what extent?

A. Well, he was manager for the Orpheum Circuit in Los Angeles prior to becoming a producer in the business, and then my brother-in-law was manager of the Keith Alby Circuit west of Denver.

Q. You are related to the Koch family?

A. Yes, I am by marriage.

Q. You know Mr. Maurice Koch?

A. Yes, I do.

Q. Do you also know Harold Koch?

A. Yes, I do.

Q. Do you know William Koch?

A. Yes, I do.

Q. Do you know the sister?

A. Yes, I do. [211]

Q. What is her married name?

A. Mrs. Abel.

Q. Right here in the courtroom?

(Testimony of David A. Sebastian.)

A. Yes, she is.

Q. Have you had transctions relating to the motion picture business with the members of the Koch family whose names you have just mentioned?

A. Yes, I have.

Q. Over what period of time?

A. The past six or seven years, I would judge, more or less.

Q. Well, this is the year 1956. In what year did your associations and affiliations with them in connection with the motion picture matters start?

A. About 1943.

Q. In 1944 did you become a member of Producers' Syndicate?            A. Yes, I did.

Q. With the Koch family and others?

A. Yes, with the Koch family.

Q. Calling your attention to matters that ran into the year 1947, I call your attention particularly to the year 1946: Did you know a Mr. David Hersh?

A. Yes, I did.

Q. Is he living now?

A. No, he is dead.

Q. He passed away? [212]            A. Yes, he did.

Q. Do you know Mr. Sam Coslow?

A. Yes, I do.

Q. Do you know where he is now?

A. Yes, he is in England.

Q. He is in England?            A. Yes, he is.

Q. Do you recall the making of a picture called 'Copacabana'?

A. Yes, I do.

(Testimony of David A. Sebastian.)

Q. Approximately when was that picture finished?

A. Approximately the first part of 1947 it was completed.

Q. Prior to the making of that film did you have activities in connection with the David Hersh whom we just mentioned?

A. Prior to the "Copacabana" deal?

Q. Yes. A. No.

Q. Was that the first picture that was made after you and Mr. Hersh got together?

A. Yes.

Q. Preceding the making of that film, did you have business dealings with your brother-in-law, Mr. Maurice Koch, in connection with your business with Mr. Hersh?

A. Prior to the making of the picture?

Q. Yes. A. Yes, we did. [213]

Q. What were those initial discussions?

A. The initial discussions were relative to the raising of funds, the moneys for the Beacon Pictures Corporation, in order to go ahead with the making of the "Copacabana" picture. I would like to add to that, if I may. The original meetings we had, Dave Hersh and I, with Mr. Koch were for the purpose of financing independent producers in Hollywood.

Q. Any particular phase of financing discussed?

A. Yes, what we termed front money, or money previous to institutional financing.

Q. Will you please talk slowly, take your time.



(Testimony of David A. Sebastian.)

and talk good and loud?           A. All right.

Q. We asked about your early discussions with Mr. Hersh and Mr. Koch in connection with the financing of motion pictures. What were your early discussions about?

A. The early discussions I had with Mr. Koch regarding the financing of motion pictures was Mr. Koch was interested in going into motion picture business, and I was to go in there and act as his agent or in his behalf and in accordance with my own specialty.

Q. Insofar as the discussions that were first had between you, Mr. Hersh, and Mr. Koch, what was the subject of those discussions?

Mr. Gillard: I object to that as calling for the opinion [214] and conclusion of the witness.

The Court: I take it it is preliminary, is it?

Mr. Fink: Yes, your Honor. I asked for the subject of the discussion.

The Witness: The subject of the discussions was the raising of funds and the advancement by H. Koch & Sons for the purpose of financing and putting up front money.

Q. What do you mean by "front money"?

A. That is the money that you use before you have your package together, that is, forming the company and acquiring rights to certain properties, and the necessary expenses that go into the first preparation before you can qualify, have a completed script and qualify for bank financing and secondary moneys.

(Testimony of David A. Sebastian.)

Q. Did you hold such discussions with Mr. Koch in the early part of 1946? A. Yes, I did.

Q. Was there any determination made at that time as to whether or not H. Koch & Sons would participate in the so-called financing of independent producers with so-called front money or preproduction money? A. Yes.

Mr. Gillard: I object to that as calling for an opinion and conclusion.

The Court: It does call for an opinion, counsel. I [215] permitted the other question because I thought it was preliminary and you were going to ask what was said.

Q. (By Mr. Fink): How many such discussions occurred, Mr. Sebastian?

A. We had quite a number of discussions.

Q. Over what period of time?

A. Over the first part of early 1946.

Q. Was this over a period of days, weeks?

A. It was over a period of months.

Q. Will you tell us what was said in those conversations over a period of months?

Mr. Gillard: I object to that.

The Court: Sustained. If you are going into what was said, let us get a conversation, counsel, and do it in the way that the rules require you to do it.

Q. (By Mr. Fink): Do you recall when the earliest of these conversations occurred?

A. I think it was the first month or two of 1946, as I recall it.

(Testimony of David A. Sebastian.)

Q. Who was present at that conversation?

A. Mr. Koch, myself and Mr. Hersh.

Q. Where did the conversation occur?

A. The first conversations we had were in Los Angeles at Mr. Hersh's house.

Q. What was said at that time? [216]

A. The discussion then was to set up the company or set up financing for the purpose of putting up the front money for independent productions.

Q. What did Mr. Koch say H. Koch & Sons would do, if anything?

A. He said they would be willing to put up a certain sum of money for this purpose, and that this fund would then be rotated.

Q. Are you able to distinguish in your mind now what conversation occurred at each one of these meetings?

A. In a general way. It is a pretty long time ago, but in a general way I believe I could.

Q. Do you recall when the second conversation took place?

A. The second conversation, I believe, took place in my office, if I recall rightly.

Q. Who was present at that time, when you say "your office"? A. I mean Mr. Fink's office.

Q. You mean the office of Fink, Ralston, Levinthal and Kent in Hollywood?

A. That is right.

Q. Who was present at that conversation?

A. Mr. Hersh, myself and Mr. Koch.

Q. Was Mr. Fink present?

A. Yes, Mr. Fink was present.

(Testimony of David A. Sebastian.)

Q. What was said at that time?

A. At that time the thought was to go ahead and set up a [217] fund for the making of this first picture, which was to be "Copacabana," and that this fund would then, after the bank loan was made, these moneys would come back and we would go in a second or third venture, using the fund on a rotating basis.

Q. The discussion was, you would rotate these funds, putting them in before the bank loan was made, and getting them repaid out of the bank loan?

A. Correct.

Q. Do you recall when the next conversation occurred?

A. The next conversation we had, if my memory serves me right, was back in San Francisco.

Q. Who was present at that conversation?

A. At that conversation was Mr. Grupp, myself and Mr. Koch.

Q. By the way, did you ever have discussions upon the subject at or about the same time with other members of the partnership, that is, other than Maurice Koch?

A. Yes, I did, prior to the meeting with Morris Grupp. I came up here before that in order to outline the proposed picture from the creative side of it, what we thought the content would be, and what we would have, and I outlined the whole production, what the ingredients of the picture would be, etc.

Q. During the balance of that year, 1946, ap-

(Testimony of David A. Sebastian.)

proximately how much time did you spend with Maurice Koch?

A. The first part of 1946? [218]

Q. Yes. A. In the first part of 1946—

Q. During the entire year, if you can describe it.

A. During the entire year I would say I spent three months in total amount, a short period or a longer time in production.

Q. In the year 1946 that would be three months or 90 days? A. I would estimate that.

Q. During that period of 90 days or three months, adding it all up, what was Maurice Koch doing?

A. Maurice Koch was helping in the preparation of passing on contracts which had to be assembled, passing on the deals being made, seeing that, as represented, the prices of things to be spent were in accordance with the budget, and what was represented to give the merchandise, the picture, under the type of release we had; it had to come in under a realistic figure.

Q. When the "Copacabana" picture was photographed, were you engaged in that work?

A. Yes, I was.

Q. What was the description of the work you did?

A. I would be assistant producer of the picture.

Q. What does the producer do in the picture?

A. The producer handles the creative end of the picture.

(Testimony of David A. Sebastian.)

Q. What did you do?

A. I was the assistant to the producer. [219]

Q. Did you also handle the creative end?

A. Yes, I did.

Q. Did the producer handle any of the financial end of that picture? A. No.

Q. Coming to the year 1947, did you have occasion to see Mr. Maurice Koch in that year?

A. Yes, I did.

Q. Did you also see other members of the Koch partnership? A. Yes, I did.

Q. What was the occasion for your seeing them?

A. I came up here regarding the Jack Chertok deal, which was the "Hill of the Hawk." I brought the books up with me. I received 30 books, and I brought some books up for them to read, so they could all read it.

Q. How much time would you say during the entire year 1947, the year in question here, did you spend with Maurice Koch?

Mr. Gillard: I object to that as incompetent, irrelevant and immaterial.

Mr. Fink: Preliminary.

The Court: Overruled.

(Question read.)

Q. (By Mr. Fink): Can you answer that?

A. Yes, I can. I would say I spent in the year 1947, the first two months, I know—I am pretty certain of that, [220] January and February, up to about the middle of March, as I recall, off and on,

(Testimony of David A. Sebastian.)

because we were still getting ready to release the picture, and then we had previews, etc., and Murray was down there for previews—there was a considerable amount of time put in down there.

Q. You mean Los Angeles?

A. Yes, Los Angeles. We were going out to preview the pictures, and we went out to preview the pictures.

Q. You said “down there.”

A. I mean Los Angeles.

Q. How much time did you spend with Mr. Koch?

A. We spent quite a period of time between January and February, just before March, and then I came up to San Francisco on about March 17th, I believe it was, if I am not mistaken, 1947, and I spent here with them about two weeks, myself and Mr. Koch, in San Francisco.

Q. After the trip here in March of 1947, did you spend any time with Mr. Koch in Los Angeles?

A. Yes, I did.

Q. To what extent?

A. To a considerable extent relative to the deal “Hill of the Hawk” and Apex Films, Jack Chertok.

Q. During the time that you spent with Mr. Koch in the year 1947, did you observe his activities?

A. Yes, I did. [221]

Q. What business was he working in?

Mr. Gillard: I object to that as calling for the opinion and conclusion of the witness.

The Court: Sustained.

(Testimony of David A. Sebastian.)

Q. (By Mr. Fink): What was he doing during all the time that you spent with him?

A. During the time he was down here we had meetings with Mr. Chertok, Mr. Mulgras, and Mr. Fink at the Friar's Club.

Q. Mr. Sebastian, you are going to have to give us some help here and take it a little bit more slowly and talk louder if you can. Get closer to the microphone. Were you connected with the matter called the "Fred Fisher Story"? A. Yes, I was.

Q. What did Mr. Koch do in connection with that matter?

A. Mr. Koch met with Mr. Al Green, the former director of "Copacabana." They had discussions regarding the making of "Hill of the Hawk." I mean, there were so many stories—"The Fred Fisher Story."

Q. How many discussions did Mr. Koch and Mr. Green have?

A. The discussions actually started during the filming of "Copacabana" and the completion of it. Mr. Green was busy. They met at the Apex Art Studios, and then Mr. Green's house, and had further discussions. Actually, even prior to that they came to an understanding. If my memory serves me right—

Q. Your understanding would not be proper to testify to. [222] A. All right.

Q. In the year 1947, I take it, the picture "Copacabana" was completed.

A. That is right.



(Testimony of David A. Sebastian.)

Q. Was it shipped off for release, to your knowledge? A. Yes.

Q. And went into release throughout the world?

A. Yes.

Q. Then, also, during the early part of that year you had discussions about the "Fred Fisher Story"? A. That is right.

Q. And the project of that picture. What was the next specific subject of discussion?

A. Insofar as picture making was concerned, picture financing was concerned, we discussed with Mr. Green the idea of actually making a series of pictures over a period of three years, which was our original discussion, and growing out of that was "The Fred Fisher Story," which was the first one we intended to go ahead with.

I would like to correct the first part of my testimony, which was the early part of 1947. I think it was a little confusing for me here.

Q. "The Fred Fisher Story" was to be the first of the series of pictures, is that correct, with Mr. Green? A. That is right, yes. [223]

Q. Subsequent to those discussions, or at the same time, whatever it may have been, did you have discussions about making other so-called Class A feature pictures? A. With Mr. Green?

Q. No, with anyone.

A. Yes, we did. We discussed after——

Mr. Gillard: Just a minute. The witness has answered the question.

(Testimony of David A. Sebastian.)

Q. (By Mr. Fink): The answer was "yes," is that correct? A. Yes.

Q. Do you recall the story "Hill of the Hawk"?

A. Yes, I do.

Q. You just told us about that. Preceding this "Hill of the Hawk" matter, were there discussions or any activities looking towards the making of a film or films? A. Yes, there was.

Mr. Gillard: Just a minute. The witness answered the question.

The Witness: Yes.

Q. (By Mr. Fink): What activity did Mr. Koch or H. Koch & Sons participate in in that respect? A. I met with Mr. Al Green.

Q. Aside from the meetings with Mr. Green and the projected series of pictures with him, were other picture activities taken up during that year by H. Koch & Sons or Mr. Maurice Koch? [224]

A. I remember one, I believe, was Desi Arnaz and Lucille Ball. That was under discussion at the time.

Q. Did that have anything to do with Mr. Green? A. No.

Q. A different project? A. Yes, entirely.

Q. Do you recall any others at or about that same time in 1947?

A. Well, in 1947 we would also have another discussion and some B pictures, which would be made at Monogram.

Q. Did Mr. Koch participate in activities relative to the Monogram pictures?

(Testimony of David A. Sebastian.)

A. Yes, he did. He worked with Mr. Fink on the contracts which were submitted and which he went over. In my presence we discussed——

Mr. Gillard: Just a minute. We object to that. The witness is now giving conversations without the foundation being laid. He has answered the question.

The Court: That is true. Direct your attention to a particular conversation.

Mr. Fink: I had in mind, your Honor, the activities, not the conversations, so we can short-cut the time we are taking of your Honor's time here.

Q. Mr. Sebastian, what was the nature of this Monogram project? [225]

Mr. Gillard: I object to that as calling for the opinion and conclusion of the witness.

Q. (By Mr. Fink): Will you describe what the Monogram project consisted of?

A. The Monogram project consisted of the making of cheap, inexpensive pictures through the release of Monogram, which Mr. Koch was to put up the financing, the front money, and Monogram was to put up the production money.

Q. Insofar as the "Hill of the Hawk" was concerned, did you have discussions on that subject in the year 1947? A. Yes.

Q. Preceding those discussions, what were the activities that led up to that discussion?

Mr. Gillard: I object to that as vague and general.

The Court: It is. Sustained.

(Testimony of David A. Sebastian.)

Q. (By Mr. Fink): With regard to the property "Hill of the Hawk"— A. Yes.

Q. —when did you first have a discussion with Mr. Koch upon the subject of the "Hill of the Hawk"? A. The latter part of 1947.

Q. Who was present?

A. Mr. Fink was present and Mr. Koch—no, I came to San Francisco without first having discussions with him, and having read the book myself, and seeing if he indicated any interest [226] in this project.

Q. Before you had this book, before you discussed the particular title "Hill of the Hawk"—

A. Yes.

Q. —did you have any discussions upon the same or similar subject matter that led up to this?

Mr. Gillard: I object to that as incompetent, irrelevant and immaterial.

The Court: I will permit that as preliminary. I take it the discussions were with Mr. Koch.

Mr. Gillard: That was not the question.

Mr. Fink: Yes.

The Witness: In the year 1947?

Mr. Fink: Yes. I will withdraw the question.

Q. Do you know Mr. Jack Chertok?

A. Yes, I do.

Q. Did you have occasion to talk with him in the year 1947? A. Yes, sir.

Mr. Gillard: I object to that as incompetent, irrelevant and immaterial.

(Testimony of David A. Sebastian.)

The Court: I will permit him to answer "yes" or "no".

The Witness: Yes.

Q. (By Mr. Fink): Where did this conversation take place?

A. It took place at the Friar's Club, it took place in Mr. Chertok's office, in Mr. Chertok's home. It took place in [227] your office, Mr. Fink. I had many conversations with Mr. Chertok.

Q. Pardon me?

A. We had many conversations with Mr. Chertok.

Q. Was Mr. Koch present at some of these conversations?

A. At the majority of them. In fact, he was at some that I was not.

Q. After you had these discussions with Mr. Chertok, did you have a talk with Mr. Koch, that is, out of the presence of Mr. Chertok?

A. Yes.

Q. Where did this conversation occur?

A. It occurred in Los Angeles and also in San Francisco.

Q. Which one occurred first, Los Angeles or San Francisco?

A. Los Angeles first, and then San Francisco.

Q. Where did the conversation in Los Angeles take place?

A. The conversation in Los Angeles took place in the Friar's Club, I believe, was the first conver-

(Testimony of David A. Sebastian.)

sation we had there. In your office was the first conversation.

Q. Who was present?

A. Mr. Fink was present, Mr. Koch was present, and I was present.

Q. What was said at that time, or approximately when was it?

A. It was approximately the latter part of 1947, as I remember; the last half of 1947, as I recall. [228]

Q. Will you tell us what was said at that time?

A. Yes. If I remember correctly, the discussion there was to set up a company for the purpose of financing, again, motion pictures in Hollywood in an independent way and also to finance Jack Chertok, and I think the instruction would be for Mr. Chertok to go East, if I recall correctly.

Q. Then did you have another conversation on the same subject after the conversation at my office?

A. Yes, we did. We discussed then using the Ambassador Films that was formed in your office for the purpose of buying "Hill of the Hawk."

Q. In the meantime, had you been to San Francisco?

A. Yes.

Q. Had you talked with members of the Koch family?

A. Yes, I did.

Q. You said something about sending Mr. Chertok East. Was there ever a discussion held with Mr. Chertok about his going East?

A. Yes.

Q. When was that?

(Testimony of David A. Sebastian.)

A. That was about the middle half, I believe, of 1947, or shortly after.

Q. Who was present at that conversation?

A. Mr. Koch, Mr. Fink and myself.

Q. Do you recall where it took place? [229]

A. That took place in your office, Mr. Fink's office.

Q. What was said to Mr. Chertok about going East?

A. To acquire the rights of property and for the purpose of making the pictures that we had in mind.

Q. To acquire property rights to make a picture? A. Yes.

Q. Was "Hill of the Hawk" mentioned until that day?

A. It was not mentioned until 1947, as I recall.

Q. Did Mr. Chertok go East? A. Yes.

Q. He returned? A. Yes.

Q. After he returned, was there a conversation held? A. Yes.

Q. Where did that conversation take place, if you remember?

A. As I recall it, the next meeting we had was with Mr. Milt Grosner, Mr. Fink, Mr. Koch and myself at the Friar's Club.

Q. Milt Grosner, do you know him?

A. Very well, yes.

Q. What is his business or occupation?

A. He is head, I believe president or vice presi-

(Testimony of David A. Sebastian.)

dent, of the G. A. C., General Amusement Company of America.

Q. What is this Friar's Club that has been mentioned several times?

A. The Friar's Club is an organization similar to Belasco's. [230] It does charitable work for members of the entertainment field.

Q. People in the entertainment world?

A. Yes, that is right.

Q. What was said at the said Friar's Club with Mr. Grosner, Mr. Chertok, Mr. Koch, Mr. Fink and yourself?

A. At this meeting there was \$7,000.00 paid into the Ambassador Pictures by Mr. Koch and \$18,000.00 paid for the purchase of the book, as I recall it.

Q. What was the total price of the book?

A. \$25,000.00.

Q. Was the book "Hill of the Hawk" mentioned at that time?

A. Yes.

Q. What was said about it?

A. The thought was it would make a very, very fine picture.

Q. Did Mr. Chertok discuss his trip to the East?

A. Mr. Chertok, I believe, had already come back from the East.

Q. After he came back, were you ever present at any conversation in which he made a report of what happened in the East?

A. No, Max, I wasn't present at that meeting. I am sorry.

Q. After this conversation and the \$7,000.00



(Testimony of David A. Sebastian.)

payment, was anything done with regard to "Hill of the Hawk" to your knowledge?

A. Yes, there was. There was a treatment made on the book, as I recall.

Q. Just how was this treatment made? [231]

A. It was made by Mr. Chertok, who hired the writers, paid for by Mr. Koch and his partners, as I understand.

Mr. Gillard: I object to the latter part and ask that it go out as the opinion and conclusion of the witness.

Mr. Fink: It may go out.

The Court: It may go out.

Q. (By Mr. Fink): Mr. Sebastian, what do you mean by "treatment"?

A. We take the book first of all. We had to get a slant on the book, because we couldn't produce the book as it was. We had to get a story line which had a beginning, a middle and an end. In order to do this, we had to eliminate some of the things in there that would not pass censure. For example, there are certain things in there that were not relevant to the true story line.

Q. Approximately how long did this preparation or treatment go on with regard to the "Hill of the Hawk" to your knowledge?

A. To my knowledge it went on approximately eight weeks.

Q. After that treatment was available, do you know whether or not Mr. Maurice Koch saw that treatment?

A. Yes, he did.

(Testimony of David A. Sebastian.)

Q. Was anything further done with regard to a screen play or treatment?

A. On "Hill of the Hawk"?

Q. Yes.

A. I believe due to the difficulties of trying to whip the [232] story and casting problems, there was a difference of opinion on the approach to the story, that Mr. Koch sold out the rights that he had in "Hill of the Hawk" to Mr. Chertok.

Q. That was about two years later, wasn't it?

A. Yes, that was two years later. I mean to say, after that he stepped out, so far as I know.

Q. Do you recall the matter of some training films or discussions on that subject in the year 1947?

A. Yes, I do.

Q. Were you present at some of the discussions on that subject?      A. Yes, I was.

Q. Where did these discussions take place?

A. The first discussion we had took place in Mr. Chertok's office, where he outlined the whole program to us, and that was about October or November of 1946, as I remember, when these came under discussion, and Mr. Koch and myself and Mr. Fink went over the whole program of these Army pictures, the contracts, etc., and Mr. Chertok was unable to finance them. That was our reason for being there and Mr. Koch's reason for being there.

Q. After these discussions with regard to the making of training films and the financing of them, were some training films made?      A. Yes.

Q. Do you know how many?

(Testimony of David A. Sebastian.)

A. I believe there were about 30 or 40. [233]

Q. Did you work on those films? A. No.

Q. You were not employed in connection with them? A. No.

Q. At times when Mr. Koch was not in Hollywood or Los Angeles, and at times when you were there in the year 1947, did you act for Mr. Koch?

A. Yes.

Q. What did you do for him or for H. Koch & Sons?

A. Primarily what I did for Mr. Koch was to sit through a vast amount of different type of productions in order to find something that was meritorious before I would submit it to him, and he would pass on it, whether he had an interest in that type of product. If he did, he took it on from there.

Mr. Gillard: I object to the latter part of the answer and request that it go out as the opinion and conclusion of the witness.

The Court: I do not know what the latter part of the answer is, counsel.

(Answer read.)

Mr. Gillard: From the point with respect to what Mr. Koch did, I move that that be stricken as the opinion and conclusion of the witness and not responsive to the question.

The Court: I think it may remain.

Q. (By Mr. Fink): So far as your own personal knowledge is [234] concerned, with regard to the year 1947, approximately what part of Mr.

(Testimony of David A. Sebastian.)

Koch's time did he spend in connection with motion picture activities?

Mr. Gillard: I object to that as calling for the opinion and conclusion of the witness.

The Court: Sustained.

Mr. Fink: We have no further questions at this time, your Honor.

### Cross-Examination

By Mr. Gillard:

Q. I do not believe you specified, Mr. Sebastian, your exact relationship to Mr. Maurice P. Koch.

A. I am his brother-in-law.

Q. Is your wife alive?

A. No, my wife passed away.

Q. Was that the relationship, that you married one of his sisters?

A. No, he married one of my sisters.

Q. He married one of your sisters?

A. Yes.

Q. In connection with the "Copacabana" affair, who first talked to you about that film?

A. About "Copacabana"?

Q. Yes.

A. It was first brought to my attention by Mr. Hersh, as I recollect. [235]

Q. At that time had Mr. Hersh already made arrangements for a picture based upon the Copacabana Club?

A. Mr. Coslow, I believe, had the release with

(Testimony of David A. Sebastian.)

United Artists for a picture—in fact, for three pictures, as I recall it, and Mr. Hersh with Mr. Coslow had obtained or, rather, through their other associates had obtained the rights, but no rights were actually paid for until Mr. Koch came into the picture. We talked about rights but no rights were actually obtained or paid for.

Q. Prior to that time, Mr. Hersh had formed Beacon Pictures Corporation, had he not?

A. Beacon Pictures Corporation was just a structure. It was not a company. There was no stock issued. It couldn't be issued because there was no money in the corporation.

Q. But the corporation had been formed?

A. Yes, but no permits or licenses for selling stock or distribution of stock had been obtained at that time.

Q. Prior to the discussions with Mr. Koch about "Copacabana," had the corporation been formed?

Mr. Fink: May I object on the ground that the witness would not know when it was formed.

The Court: If he does not, he may say so.

The Witness: I don't know when it was formed. I mean, actually when the Articles of Incorporation were taken out, I don't know. [236]

Q. (By Mr. Gillard): Prior to the time you first talked to Mr. Koch about this affair, didn't Mr. Hersh tell you that he had already formed Beacon Pictures Corporation?

A. They mentioned they had Beacon Pictures Corporation, yes.

(Testimony of David A. Sebastian.)

Q. And thereafter Mr. Hersh was desirous of forming a partnership with you, and that was for the purpose of promoting Beacon Pictures Corporation and the "Copacabana" film?

A. Mr. Hersh was desirous of forming a partnership with me, yes.

Q. And you did so? A. And we did so.

Q. I will show you a document entitled "Articles of Copartnership," dated July 23, 1946, and ask you to look at the last page thereof. Is this a photostatic copy of that? A. Yes.

Q. Would you like to look over that document and see if that is a partnership agreement that you formed with Mr. Hersh at that time?

A. It has my signature on it, so I would assume it is. My signature is here. I recognize David Hersh's signature and mine.

Mr. Gillard: I will offer it in evidence as defendant's next in order. It is a partnership agreement.

The Court: Exhibit J.

(The document referred to was thereupon received in evidence and marked Defendant's Exhibit J.) [237]

Q. (By Mr. Gillard): Your first discussions with Mr. Koch were for the purpose of getting some capital for the partnership of Hersh and Sebastian, were they not, Mr. Sebastian? A. No.

Q. Did you receive any money from Mr. Koch in the early part of 1946? A. Yes.

Q. Specifically when and how much?

(Testimony of David A. Sebastian.)

A. I received approximately—you mean all the total funds that went through me?

Q. What was the first amount that you received, Mr. Sebastian?

A. The first amount I received was \$15,000.00, if I remember rightly.

Q. Do you remember when that was?

A. That was in the early part of 1946, some time in 1946.

Q. That was a personal loan to you, was it, Mr. Sebastian?

A. No.

Q. What was it?

A. \$10,000.00 of it was to go to Hersh & Coslow for the money to put into the company—in other words, it was the vehicle in order to assemble and obtain the release, because without the money in there, there was no way of obtaining a release of the picture “Copacabana.” So the money was given to Hersh and Coslow, \$7,500.00, and then there was another \$2,500.00, in addition to the \$5,000.00 which was left of the \$15,000.00, [238] which was to defray the expenses which we entailed in behalf of Murray Koch prior to actual production.

Q. Let us go over this a little more slowly, sir. I will show you Exhibit No. 6. The first amount of money you received was a check made payable to your order and issued by Murray P. Koch, on behalf of H. Koch & Sons?

A. Yes.

Q. Was there any agreement executed with reference to the \$15,000.00 between you and Mr. Koch?

(Testimony of David A. Sebastian.)

A. Not to my knowledge, or I don't remember.

Q. Was there ever anything in writing as to what the purpose of that \$15,000.00 was?

A. No, not to my knowledge, not to my exact knowledge, no.

Q. The money was paid to you to dispose of in accordance with your desires?

A. No, under the direction of Mr. Koch.

Q. Under the direction of Mr. Koch?

A. Yes.

Q. Who was responsible to repay Mr. Koch for that \$15,000.00?

A. May I tell you in my best way?

Q. I just want you to answer that question, Mr. Sebastian.

A. Thank you. The \$10,000.00 went in to activate the corporation.

Q. I asked you who was responsible to repay the \$15,000.00 to Mr. Koch represented by that check. [239]

A. There is a chain of events here, Mr. Gillard. The \$10,000.00 was to be repaid out of the dissolution—when the picture was finished and profits came in, etc., and the corporation was then dissolved. The \$10,000.00 which went in to pay for Hersh and Coslow were to come back to Mr. Koch. The \$7,500.00, which was another \$2,500.00, I believe, that was paid in addition to the \$15,000.00—I notice there is \$7,500.00, but there was another \$2,500.00 paid, I am sure—that went to Hersh and Sebastian to defray the expenses that were entailed in the preproduction work.



(Testimony of David A. Sebastian.)

Q. The other check that you referred to is Exhibit 8 herein, a check made also to your individual favor for \$2,500.00 by Maurice P. Koch on behalf of H. Koch & Sons? A. Yes.

Q. Out of the total of that \$17,500.00, \$7,500.00 was loaned directly to you, was it?

A. No, it was not loaned to me.

Q. It was loaned to Hersh & Sebastian?

A. No.

Q. To whom was it loaned?

A. It was not loaned. It was to defray the expenses which we entailed. We were employed at the time working for Mr. Koch.

Q. You were working for Mr. Koch?

A. We were agents of his, yes, and there were expenses entailed in there that we had been out of pocket for, meetings with him, [240] phone calls, etc., and this was to defray part of the expense.

Q. Who was responsible to pay that money back to Mr. Koch?

A. The \$7,500.00, as I recall—we'll take the \$7,500.00—the \$7,500.00, as I recall it, would have been returned to Mr. Koch out of the profits of the picture. In other words, if I remember, I think Mr. Koch received a pro rata percentage points for the \$7,500.00 which were to come out when the corporation was dissolved, which would come out of the profits of the corporation. But we ourselves were not held responsible for this. In other words, it was to come out of our share of the profits, but there was nothing that I know of in the papers drawn of these amounts being owed him, as I recall.

(Testimony of David A. Sebastian.)

Q. Was there any agreement drawn between you and Mr. Koch indicating you were not personally responsible for this money that was given to you?

A. Not to my knowledge.

Q. In the partnership of Hersh & Sebastian, did you put up any money for the capital of that partnership?

A. For Hersh & Sebastian?

Q. Yes.

A. No, I didn't put up anything.

Q. You put in nothing?

A. No.

Q. I refer you, sir, to paragraph 6 of your partnership agreement, Exhibit 5 in evidence [241] herein.

“Sebastian shall contribute to the partnership as capital cash in the sum of \$75,000.00, which shall be reflected as his contribution to the capital account of the partnership. It is acknowledged that of that said sum the sum of \$10,000.00 has heretofore been contributed to and for partnership purposes by Sebastian, and that said amount has heretofore been delivered to Hersh.”

A. The \$75,000.00 did not go for the partnership, Mr. Gillard.

Q. How about the \$10,000.00, Mr. Sebastian?

A. The \$10,000.00 did not go through the partnership.

Q. What, sir?

A. The \$10,000.00 did not go through the partnership?

Q. It is did not go through the partnership?

A. No, sir.

(Testimony of David A. Sebastian.)

Q. What does this phrase mean?

A. That was, I believe, the original deal we had between Mr. Hersh and myself in order to safeguard these funds, and in talking with Mr. Koch. After that I believe Mr. Koch went direct to the principals themselves and made his own deal apart from us. I had nothing to do with the percentage points Mr. Koch received, or his participation in "Copacabana," or future investments that he made in "Copacabana." The only funds I received was the amount of \$7,500.00, which I received half of it from the Hersh-Sebastian partnership. Other than that, there [242] was no money that went into the Hersh-Sebastian partnership that I know of.

Q. Let me read this again: "It is acknowledged that of the said sum, the sum of \$10,000.00 has heretofore been contributed to and for partnership purposes by Sebastian." That is not true, sir?

A. I imagine it is if it says it there, but I paid the check myself, a personal check from the \$15,000.00 Mr. Koch gave me, which had been deposited in my own bank account, not the partnership bank account, and I made that check payable to Sam Coslow and Hersh.

Q. Isn't it true, Mr. Sebastian, of that \$15,000.00 which is represented by Exhibit 6 in front of you, you contributed of that amount \$10,000.00 to the capital of Hersh & Sebastian as recited in this agreement?

A. Well, I will have to stand on the record, what it says there, Mr. Gillard.

(Testimony of David A. Sebastian.)

Q. Thank you. I will show you, sir, Exhibit 15 in evidence, being a letter signed by you and Mr. Hersh dated August 12, 1946. There again the \$10,000.00 is referred to, is it not, sir? Would you read that middle paragraph, Mr. Sebastian?

A. "The \$10,000.00 originally advanced to Dave Sebastian and subsequently turned over to me for capital investment in Beacon Pictures will be taken care of by the Hersh-Sebastian partnership interest in Beacon Pictures." [243]

Q. Was there anything said in there about the remaining \$7,500.00 that was advanced to you?

A. No, I don't see anything here.

Q. Did you ever reach any agreement with Mr. Koch not to repay him that \$7,500.00 in writing?

A. Not to my knowledge.

Q. Did you ever make any agreement with him not to repay the \$10,000.00?

A. Not to my knowledge.

Q. Prior to the formation of the Hersh-Sebastian partnership, you had been employed in Hollywood, had you? A. Yes.

Q. By whom were you employed?

A. I was with Columbia at the time.

Q. When did you leave Columbia?

A. I left Columbia Pictures in late 1945 or early 1946, I believe, if my memory serves me right.

Q. What was your intended occupation after leaving Columbia?

A. I went on to Beacon Pictures, went into "Copacabana" with Mr. Koch.

(Testimony of David A. Sebastian.)

Q. With Mr. Koch or Mr. Hersh?

A. Well, with Mr. Koch and Mr. Hersh.

Q. Your intended occupation after leaving your salaried position was to engage as an independent producer?

A. No, that is impossible for me to have been an independent [244] producer. First of all, the deals were already set up, and those are the deals I went into. I went in as Mr. Koch's agent, and my specialty has always been where people don't understand the full techniques going into the making of the picture. I am the safety man put in there for the purpose of guiding. I did that many times. I did that with directors from New York. That was my specialty, on the creative side of it.

Q. Wasn't it intended that you be the producer of "Copacabana"? A. Definitely not.

Q. With reference to any other deals besides "Copacabana," what was your intended profession after leaving Columbia Pictures?

A. I only left Columbia Pictures at the time we made "Copacabana." That was the only time that I left, and I couldn't have been producer of "Copacabana" because I didn't have the release. Mr. Coslow did.

Q. I am not referring merely to that one picture, sir. In addition to "Copacabana" you had other plans, did you not? A. Yes, we did.

Q. Wasn't this your idea, Mr. Sebastian, that by virtue of your professional background you would at least be associate producer in pictures?

(Testimony of David A. Sebastian.)

A. I have never been an associate. I have been an assistant to the producer.

Q. You were looking, were you not, for opportunities to become an assistant or a producer? [245]

A. Definitely.

Q. It was your object to scout around and try to find deals on which you could make money as a producer or the associate producer of those pictures?

A. If I could build to that, yes. But you can't do that just for the asking.

Q. For that purpose you had the prospective financial assistance from your brother-in-law to put up the pre-production money for whatever opportunities you found that you saw fit to go into?

A. Mr. Koch selected all the deals we went into. It was not my selection.

Q. Weren't you the one who turned down the "Hill of the Hawk," Mr. Sebastian?

A. I turned down the treatment, not the book.

Q. You turned down the idea?

A. Also, Mr. Koch went on with the deal. I left it completely and Mr. Koch carried it on.

Q. Prior to that time hadn't you advised against going into that as a motion picture production because of the treatment of the book?

A. Prior to the purchase of the book? No, I submitted the book to Mr. Koch.

Q. With the recommendation that——

A. That we go ahead with it.

Q. Pardon me, sir, if I may finish my question.

(Testimony of David A. Sebastian.)

After the [246] story treatment on the book that you have referred to, you recommended to Koch that he not go into that deal, isn't that correct?

A. Upon my return from Europe, and I read the treatment in Europe, yes. After I saw the treatment, I recommended to him that I did not feel that they had followed the story line as we had discussed here, yes, before I left.

Q. And with reference to these other matters that you referred to on your direct examination, you said you had gone through piles of materials looking for good story material for the making of the picture?

A. I have in my home about 500 scripts, Mr. Gillard.

Q. You were looking at this for the purpose, one, of securing vehicles in which you could produce, if Koch would finance, isn't that correct?

A. Not at all, Mr. Gillard.

Q. What was your part to be?

A. I have served many times in any capacity. I was building towards that, yes, but I was serving. It was impossible for me—if I had a million dollars—to go down there as a producer automatically.

Q. What salary was Mr. Koch paying you?

A. Mr. Koch was paying my expenses and providing a job for me in any production we went into. That was my deal with him.

Q. No salary? [247]                      A. No salary.

Q. Any ventures that you went into, the opportunity was to be yours to make your living in some

(Testimony of David A. Sebastian.)

fashion in connection with the production of that picture?

A. Provided it promoted my career, yes.

Q. Provided he put up the pre-production money, isn't that correct? A. Yes.

Q. You were not an agent of Mr. Koch's, were you? A. Yes, I was.

Q. You were not paid by him?

A. Mr. Koch compensated me by providing for me a job within the production itself. The jobs that I would get would be step-ups, as we planned it, until ultimately I would be producing one day. However, you couldn't start at that point.

Q. What production did Mr. Koch ever own?

A. He owned—he was a big share owner in “Copacabana” and a very important one.

Q. He owned that?

A. He was a big owner of “Copacabana.”

Q. It was owned by Beacon Pictures Corporation, wasn't it?

A. Of which he was one of the major—he held a major interest.

Q. He held some stock in Beacon Pictures Corporation? A. Not to my knowledge. [248]

Q. What other production did Mr. Koch own?

A. Well, of course, might I digress a little?

The Court: Just answer the question.

The Witness: What stage do you mean? Production to us is the purchase of a book, and I am in production. I don't know where you mean. If you



(Testimony of David A. Sebastian.)

mean a completed picture, that is the only one I know of that was completed, yes.

Q. Did you ever repay the \$17,000.00 to Mr. Koch?      A. No, sir.

Q. Did he ever ask for it?      A. No, sir.

Q. I think you mentioned that this \$10,000.00 that was turned over by you to Mr. Hersh and Coslow, was it?

A. To Hersh and Coslow, yes.

Q. Was that for the purpose of buying stock?

A. For them to buy their stock. Mr. Coslow didn't have the stock. He couldn't get the release. That was the condition of the release.

Q. Was the stock purchased?

A. So far as I know, it was. I mean, I wouldn't know, Mr. Gillard.

Q. You do not know if any stock was issued to Mr. Hersh and Mr. Coslow for that \$10,000.00?

A. I assumed it was. I don't know. I never saw an exchange of stock or stock issued, no. [249]

Q. Did you lend any money or did you or the partnership of Hersh & Sebastian lend any money to Beacon Pictures Corporation?

A. I believe the \$10,000.00, yes, that was given to the corporation by Hersh & Sebastian, so far as I know.

Q. When Beacon Pictures Corporation folded, did you file a claim in bankruptcy for your one-half interest in that \$10,000.00?      A. No, I did not.

Q. Did anybody on your behalf file such a claim in bankruptcy?      A. No, not to my knowledge.

(Testimony of David A. Sebastian.)

Q. You are positive of that?

A. To my knowledge, Mr. Gillard.

Mr. Gillard: I will offer in evidence a certified copy of the Schedule in Bankruptcy, the referee's claim register, listing the claims filed against Beacon Pictures Corporation.

Mr. Fink: With respect to the apparent purpose for which it is now offered, your Honor, we object on the ground certainly under the law a stockholder or one who is entitled to get money on the dissolution of a corporation by reason of the retirement of stock, certainly has no claim in bankruptcy against the corporation, so whether or not a claim was or was not filed could not possibly make any difference in our case.

The Court: You are offering it for what purpose, Mr. Gillard?

Mr. Gillard: For the purpose of impeaching the witness on his testimony that a claim was not filed. [250]

The Court: It may be introduced for that purpose and marked Exhibit K.

(The document referred to was thereupon received in evidence and marked Defendant's Exhibit K.)

Mr. Fink: May I ask, for the record, your Honor, that we may be entirely clear on this matter. It is clear in this record the only question asked of the witness is whether a claim was filed for the \$10,000.00 in stock.

(Testimony of David A. Sebastian.)

The Court: Or for his half of it.

Mr. Gillard: I did not phrase the question that way. That is correct.

Mr. Fink: There is no impeachment in this record, I do not believe, your Honor, based upon the way the questions went in and the answers were given.

Mr. Gillard: I would prefer to have the reporter read it back.

(Record read.)

Mr. Gillard: Will the Court indulge me a second?

Mr. Fink: May I add to my objection, your Honor, that no foundation has been laid for the introduction of the recent document?

Mr. Gillard: That is all for the moment, your Honor.

Mr. Fink: May I have the last exhibit, counsel?

### Redirect Examination

By Mr. Fink:

Q. Mr. Sebastian, Beacon Pictures Corporation went into bankruptcy, is that correct?

A. Yes.

Q. At the time they went bankrupt, did they owe you some money?      A. Yes.

Q. What for?      A. For services rendered.

Q. How much do they still owe you that was unpaid at the time of the bankruptcy?

(Testimony of David A. Sebastian.)

A. I believe it was around \$2,500.00 or \$5,000.00, something like that—\$2,500.00 something.

Q. I will show you here Exhibit K, which counsel has introduced in evidence without showing it to you, and which seems to be the claims register, Beacon Pictures Corporation, Bankruptcy Case No. 47748-WM. It shows here a claim September 15, 1949, the date of filing. Claim No. 5: David Sebastian, 616 North Bedford, Beverly Hills, \$5,000.00.

A. That is for salary owed me.

Q. Speak up, Mr. Sebastian.

A. That was a deferment which I gave during the course of the picture. My salary was \$7,500.00. \$2,500 of that I drew and \$5,000.00 of that I deferred.

Q. Did they owe you that when they went broke?

A. Yes.

Q. By the way, you hold some other claim in this bankruptcy. Carmen Miranda was your wife, is that correct? [252]

A. That is correct, yes.

Q. You were married to her after the picture "Copacabana" was made?

A. Yes.

Q. There is a claim also in this bankruptcy that you are administering in connection with this same picture?

A. Yes.

Q. So far as Beacon Pictures Corporation is concerned, after it went bankrupt, did you ever get back the \$17,500.00 from Beacon?

A. No.

Q. Or any part of that \$17,500.00?

A. No.

Q. Did you ever transmit money for H. Koch & Sons?

A. Yes.

(Testimony of David A. Sebastian.)

Q. I note that certain of the checks in evidence here for \$30,000.00, \$50,000.00 and other amounts were made payable to you. When you got those moneys, what did you do with them?

A. In some cases they were deposited to the partnership. In other cases they were given directly to Beacon Pictures.

Q. When it came to giving these notes, Exhibits 12 and 14, first for \$50,000.00 and the second for \$30,000.00, I notice they are made out to the order of Murray P. Koch. A. Yes.

Q. Did you ever get any notes from Beacon Pictures Corporation? [253] A. No.

Q. I noticed that you mentioned your activities, I believe you termed them, were on the artistic or creative side. A. Yes.

Q. Insofar as determining what part of the particular picture Mr. Koch was going to own or not own, or H. Koch & Sons was going to own, did you negotiate those percentages or amounts?

A. No.

Mr. Fink: No further questions.

Mr. Gillard: Just one further question.

Mr. Fink: I think I should as a matter of record, your Honor, move to strike Exhibit K. I do not think it has any impeachment value. If it had been shown to the witness, and he had had a chance to explain, I do not think it would have been offered in the first place.

The Court: The objection may go to the weight of the testimony or the exhibit. It may remain in evidence.

(Testimony of David A. Sebastian.)

### Recross-Examination

By Mr. Gillard:

Q. Mr. Sebastian, the latter two checks that were referred to by Mr. Fink, the one for \$50,000.00 and the one for \$30,000.00, were received by you with specific instructions, were they not, from Mr. Koch for transmittal to Beacon Pictures Corporation?

A. For transmission to Beacon Pictures Corporation, correct, yes. [254]

Q. For the purpose of consummating a loan between that corporation and Mr. Koch directly, isn't that true?      A. And the Koch people, yes.

Q. As a matter of fact, before you deposited that check to your bank account, that \$50,000 check to your bank account, you had written to him and told him you were going to do so and asked for permission to do it in that fashion, so that the money could be held until the transaction was completed with Beacon Pictures Corporation, is that so?

A. If the record shows that. I don't recall writing the letter, no. If the record shows that.

Mr. Gillard: The letter is in evidence. I can't put my finger on it right now. Thank you.

### Further Redirect Examination

By Mr. Fink:

Q. Mr. Sebastian, so we may have our play on words here clarified, what did Mr. Koch or H. Koch & Sons get for all this money as far as the picture

(Testimony of David A. Sebastian.)

“Copacabana” is concerned? Did they get just a loan or was there something more than that?

Mr. Gillard: I object to that as calling for the opinion and conclusion of the witness. The document is the best evidence.

The Court: Sustained.

Mr. Fink: I suppose I am a little late in making the objections, your Honor, but I would like to have the last questions that were asked of the witness objected to and the answer stricken for the purpose of the objection, due to the fact that they also call for the conclusion of the witness, and since we cannot clarify it, perhaps the record should be [255] clarified in that regard.

The Court: The answers may stand. They came in without objection.

Mr. Fink: We have no further questions.

Mr. Gillard: That is all.

The Court: We will take a recess now.

(Recess.)

### REBECCA KOCH ABEL

called as a witness on behalf of the Plaintiffs, being first duly sworn, testified as follows:

#### Direct Examination

By Mr. Fink:

Q. Mrs. Abel, you are the sister of Mr. Maurice Koch?  
A. Yes.

Q. And of Harold and William Koch?

(Testimony of Rebecca Koch Abel.)

A. That is right.

Q. And you are a partner in H. Koch & Sons?

A. Correct.

Q. This partnership started, I take it, in 1941?

A. The beginning of 1942.

Q. We have here in evidence as Exhibit 1 the partnership agreement, which is dated December 31, 1941.

A. That is right.

Q. You started in business in 1942?

A. January 1st, 1942. [256]

Q. Your partnership agreement was amended on or about the 23rd day of October, 1944?

A. That is right.

Q. Since this business was inaugurated beginning with the year 1942, who was the general manager of H. Koch & Sons?

A. Murray Koch.

Q. Murray, also known as Maurice?

A. Known as Maurice P. Koch, yes.

Q. Were you active in this business?

A. Yes, I was.

Q. What were your duties?

A. The office work and their books.

Q. And your other two brothers, what did they do?

A. William Koch and Harold Koch took care of the plant management and the general running of the plant.

Q. I am afraid we are having trouble hearing you, Mrs. Abel. Will you speak slowly and as loud as you can?

A. Thank you.

Q. You say that Harold and William Koch took



(Testimony of Rebecca Koch Abel.)

care of the plant?           A. That is right.

Q. I take it your business in 1946 was somewhat smaller than it is now?           A. Quite a bit.

Q. In 1946 and 1947 where was H. Koch & Sons' principal office located? [257]

A. 73 Beale Street, San Francisco.

Q. Did you occupy space in that building?

A. Yes, we did.

Q. What floor were you on?

A. We had the three floors, I believe—1946 and 1947 you said, did you not?

Q. Yes.

A. Yes, we had the three floors. I can't remember whether we had the ground floor at that time or not.

Q. At that time the business, going back to 1942 and 1943, your business was the manufacturing of luggage?           A. That is right.

Q. Did you also buy and sell luggage from other people?           A. Yes, we did.

Q. At the present time do you still make the same kind of luggage?

A. No, we do not. We are making fiberglass luggage today, which is entirely different.

Q. In other words, following the last several years you have been more or less in the fiberglass business?           A. That is right.

Q. And your business, I take it, now is larger than it was in the days of 1946 and 1947?

A. That is correct.

Q. Did your business, since you told us you were

(Testimony of Rebecca Koch Abel.)

in charge of [258] the books and records in the office in 1946 and 1947, did you keep regular business records?      A. Yes, we did.

Q. Did you supervise those books yourself?

A. Yes.

Q. Did you keep books and records of your business transactions?      A. Yes, we did.

Q. Were you in the years 1946 and 1947, in addition to the luggage business activities, also engaged in the motion picture financing business?

A. Yes, we were.

Q. Did you keep records of your transactions in connection with motion pictures?

A. Yes, we did.

Q. Were you the bookkeeper all during the year 1946?      A. Yes, the year 1946.

Q. In 1947 did you leave the business?

A. Yes, I did. I left in about March or April, 1947.

Q. Were you married at that time?

A. I went to South Africa.

Q. Did you continue to be a partner?

A. Yes, I did.

Q. And then you returned to this country?

A. Yes, in 1954, in March. [259]

Q. Did you resume the supervision of the bookkeeping since that time?      A. Yes, I did.

Q. Do you know, at least up to the time that you left, the books and records of H. Koch & Sons?

A. Yes.

Q. Since this matter has come up have you for

(Testimony of Rebecca Koch Abel.)

counsel and for us looked up the old books and records?      A. Yes, I have.

Q. Do you have them here in the courtroom?

A. Yes, I have.

Q. Will you turn to Account No. 40, please? Do you need both of these?      A. No, I do not.

Q. You have handed me here the ledger page Account No. 40. It is headed "Investment," is that correct?      A. That is correct.

Mr. Fink: Counsel, you have a copy of this page, have you not?

Mr. Gillard: I believe I have a photostatic copy of it.

Q. (By Mr. Fink): The first item on this page appears to be May 31st, and let me ask you this: On this particular page is it customary to make the entries only at the end of the month?

A. Yes, it is.

Q. In other words, transactions prior to this page are added [260] up at the end of the month?

A. Yes.

Q. I notice each entry here seems to be for the end of the month.      A. Yes.

Q. On May 31, 1946, the end of that month, we see "CR 259 \$17,500."

A. Yes, that represents a check issued. I say that represents a check issued.

A Juror: If the lady would talk into the microphone——

Q. (By Mr. Fink): The \$17,500 represents what?      A. A check issued.

(Testimony of Rebecca Koch Abel.)

Q. The "CR" represents——

A. Check 259.

Q. "CK," what does that refer to?

A. That is the check record 259.

Q. Do you have the check record here?

A. Yes, I do. There it is, \$17,500.

The Court: Please. You are either speaking for the record or not.

The Witness: That \$17,500 represents a check issued on May 17th to D. Sebastian for \$15,000, and the other check here is issued on the 22nd for \$2,500 to D. Sebastian.

Q. (By Mr. Fink): And the \$15,000 check and the \$2,500 check total the sum of \$17,500, is that correct? [261] A. That is correct.

Q. That was entered at the end of the month on this page? A. Check 259, that is correct.

Q. Are there any matters on this page, Account 40, that do not pertain to the picture business?

A. Yes, there are.

Q. Will you tell us what they are?

A. There is one item down here, \$66,000, which was the land that we purchased over in Corte Madera.

Q. Was that your factory land?

A. That was our factory land, yes, and the real estate tax on it for \$287.00 is there as well.

Q. You have your factory property where your factory is located now? A. That is correct.

Q. And the taxes on that land in the year——

A. 1953.

(Testimony of Rebecca Koch Abel.)

Q. 1953, and aside from that everything else on that page relates to motion pictures?

A. That is correct.

Q. We see here an item of \$50,000 put down here at the end of the month of August, 1946.

A. That is from check record 270, and it is issued on the 5th of August, payable to D. Sebastian for \$50,000.

Q. The next one is \$30,000, which is entered in the month of [262] October as far as Account 40 is concerned?

A. Then there is a check issued on the 17th of October—pardon me—on the 16th of October to D. Sebastian for \$30,000.

Q. And we have on November 30th, 1946, an entry here of \$20,000 at the end of that month.

A. That was a check that was issued on the 22nd and made payable to Beacon Pictures.

Q. These checks that you told us about so far are all from H. Koch & Sons, a copartnership?

A. That is correct.

Q. The next entry seems to be—now, that last item of \$20,000, I see an item of \$20,000 on December 31st as a credit. What does that indicate?

A. That was money received on the 31st of December. That is in the cash record. That was a check of \$20,000 returned from Beacon Pictures.

Q. Beacon Pictures paid you back \$20,000?

A. That is correct.

Q. That was December——

A. December 6th.

(Testimony of Rebecca Koch Abel.)

Q. December 6, 1946?      A. Correct.

Mr. Fink: Your Honor, I should like to offer in evidence page 40 taken from the ledger, and I should like to ask leave of Court to substitute a photostatic copy of this page in order [263] that the books may be returned intact.

Mr. Gillard: So far, if the Court please, the testimony that has been elicited from this witness and the record of the investment account that she has read off merely duplicates the checks that have been put in evidence and the testimony of Mr. Koch. I do not know that this adds anything.

The Court: The photostatic copy may be admitted in evidence and marked Exhibit 37.

Mr. Gillard: May I pass up a photostatic copy to the Court for a minute? The evidence was that there were transactions on there which did not pertain to the motion picture business, and also there are transactions on there in 1948 which were excluded from the testimony at a prior time. I would assume that the record of this investment account 40 should be put in evidence limited to time.

Mr. Fink: At counsel's request I will be glad to withdraw the exhibit, if I may do so, since we apparently do have our checks in evidence and testimony in regard to these transactions already in the record.

The Court: Then you do not desire the exhibit introduced?

Mr. Fink: I think I would just as soon withdraw it and not encumber the record further.

(Testimony of Rebecca Koch Abel.)

The Court: The order admitting it may be set aside.

Q. (By Mr. Fink): I would like to have you take a look at Account No. 2, the year 1947. [264]

A. Account No. 2. I have the photostatic copy only.

Q. What was the cash position of H. Koch & Sons at the end of the year 1947?

A. At the end of 1947 we show overdraft, Pacific National Bank, of \$14.14.

Q. Did you have any other bank accounts?

A. No, we did not.

Q. That was your only bank account?

A. Yes.

Q. At that time how much money did you have invested in the picture business?

A. At the end of 1947 we had \$75,000.

Q. At the end of the month of October, 1947, what was the cash position of H. Koch & Sons?

A. October, 1947?

Q. October 31st.

A. We have an overdraft of \$808.01.

Q. At that time how much did you have invested in the picture business?

A. \$82,500.

Mr. Fink: That is all.

(Testimony of Rebecca Koch Abel.)

Cross-Examination

By Mr. Gillard:

Q. Mrs. Abel, you have given us certain figures with reference to the investment of H. Koch & Sons in the motion picture business, and excluding the item of \$20,000, [265] which was paid out in November and repaid in December, those two items cancelled each other, is that correct?

A. That is correct.

Q. The balance of the total investment shown by this account then was \$97,500?

A. That is correct.

Q. The balance of the total investment paid out?

A. At what period?

Q. I am just now taking the investment side of the ledger, Mrs. Abel.

A. \$97,500. You are correct.

Q. That is correct. You later testified from, I think you said, Account No. 2 that the investment at the end of 1947 was \$75,000 and at the end of October, 1947, the investment was \$82,500.

The Court: I think your dates are incorrect, Mr. Gillard. I do not think you mean at the end of 1947 they were \$75,000.

Mr. Gillard: Maybe I misunderstood the witness.

Q. What was your testimony as to the amount shown in Account No. 2 as the investment of H. Koch & Sons as of December 31, 1947?



(Testimony of Rebecca Koch Abel.)

Mr. Fink: Counsel, No. 2 is the bank account. Do you want a copy of it?

Mr. Gillard: You are testifying from some other record.

Mr. Fink: Account No. 40 is the investment account. [266]

Mr. Gillard: You gave a figure as to the investment of H. Koch & Sons as of the end of 1947.

The Witness: No, 1946.

The Court: You gave another figure at another time, October, 1947.

The Witness: That is correct. October, 1946, I believe it was.

The Court: You gave a figure of \$82,500.

The Witness: That was as of October 31, 1946.

Q. (By Mr. Gillard): Did you give a figure of \$75,000? A. Yes, I did.

Q. For what was that?

A. That was at the end of October, 1946.

The Court: I don't understand. You just said that at the end of October, 1946, it was \$82,000. Now you say \$75,000.

A. October it was \$82,000. December 31st it was \$75,000.

Q. You said October both times.

A. I am sorry.

Q. (By Mr. Gillard): In other words, it is your testimony that the records show that during the year 1946 a decrease in the total original investment of \$97,500 took place, is that correct?

(Testimony of Rebecca Koch Abel.)

A. I didn't quite follow the question.

Q. Your testimony shows a decrease in the total amount invested during the year 1946.

The Court: Decrease from what, counsel? [267]

Mr. Gillard: Decrease from \$97,500.

The Witness: To \$75,000 correct.

Q. (By Mr. Gillard): The decreases are shown by the entries in the credit account on investment account No. 40, is that correct?

A. That is correct.

Q. Investment account No. 40 is not what you call an original account, is it, Mrs. Abel?

A. Just what do you mean by an original account?

Q. It is an account which is taken from other accounts, which are the original accounts.

A. The postings in the Account No. 40, investments, are drawn from the general journals of the books.

Q. And those would be considered the original accounts?

A. The original entry. This is the control book.

Q. The first decrease in the investment of H. Koch & Sons which is shown on investment account No. 40 was made with an entry on June 30, 1946, in the amount of \$5,000, is that correct?

A. That is correct.

Q. That was taken from your cash receipts record on page 102? A. That is correct.

Q. Will you turn to cash receipts record, page 102, and tell me where that \$5,000 came from?

(Testimony of Rebecca Koch Abel.)

A. That consist of two checks, one check for \$2,500 on the 18th of June from F. Farilla and one from R. Haller for \$2,500. [268]

Q. The next item on your investment account 40 as of August 31st shows a credit to the account of \$2,500. That came from your accounts receipts register, page 107. Where did that money come from?

A. That was the cash receipts on the 22nd of August from Roy Haller.

Q. The next item on the investment account, \$7,500, posted as of October 31, 1946, in the amount of \$7,500, that came from cash receipts record, page 112, where did that money come from?

A. That was a check on the 8th of October from F. Farilla.

Q. For \$7,500?            A. \$7,500.

Q. And the last entry, disregarding the canceling \$20,000 entries, is an entry on December 31, 1946, for \$7,500, and that came from cash receipts at page 117, will you tell us what that entry is for?

A. That is on the 27th of December. There is a check for \$2,500 from Roy Haller, one for \$5,000 from F. Farilla.

Mr. Gillard: Thank you.

### Redirect Examination

By Mr. Fink:

Q. Mrs. Abel, in addition to the money of H. Koch & Sons that was used in this picture business, did you likewise use money borrowed or obtained from other people?            A. Yes, we did.

(Testimony of Rebecca Koch Abel.)

Q. Some of this money was obtained from a man named F. Farilla. [269] Was that Frank Farilla?

A. That was obtained by Maurice Koch, yes.

Mr. Gillard: I am going to ask that the answer go out to allow me to make an objection. The witness obviously is not testifying from her own knowledge on that.

The Court: The motion may be denied. It came in without objection.

Q. (By Mr. Fink): Then some additional money that shows as having come from—what was the other name? A. Roy Haller.

Q. Roy Haller. Do you know of your own knowledge whether or not H. Koch & Sons were seeking funds from other people to assist in this business of motion picture financing? A. Yes, we did.

Q. Pardon me? A. Yes, we did.

Q. In any event, so far as your books reflect, did you ever get back \$80,000 from a picture called the "Copacabana"? A. No, we did not.

Q. The suit here in question has to do with a loss incurred in 1947 by the partnership in the sum of \$75,000. A. That is correct.

Q. However, the notes which we have in evidence here indicate the sum of \$80,000 was advanced in connection with the picture "Copacabana." Can you tell us what this \$5,000 differential is? [270]

Mr. Gillard: I object to that as calling for the opinion and conclusion of the witness.

The Court: Overruled.

(Testimony of Rebecca Koch Abel.)

Mr. Fink: Insofar as your records are concerned. May I reframe the question?

The Court: Do you understand the question?

The Witness: No.

Q. (By Mr. Fink): How much money did you get from Roy Haller altogether?

A. \$5,000—yes, \$5,000.

Q. \$5,000? A. I believe so.

Q. I see by your records here in connection with this "Copacabana" \$17,500—

A. I am sorry, there is another \$2,500 in here.

Q. Did he get part of that back? A. No.

Q. That was his money, is that correct?

A. That is correct.

Q. You never treated that as partnership funds, Mr. Haller's money? A. No, we did not.

Q. So we have no concern about that here.

A. That is correct.

Q. You received approximately, I think, in accordance with [271] figures counsel mentioned, around \$15,000 from Frank Farilla, is that correct?

A. That is correct.

Q. Were there any changes made with regard to that money after it was noted as Frank Farilla?

A. Yes, sir.

Mr. Gillard: I object to that as incomprehensible.

The Court: Do you mean changes on the books?

The Witness: Yes.

The Court: You may answer.

The Witness: Yes, there were.

(Testimony of Rebecca Koch Abel.)

Q. (By Mr. Fink): What changes were made?

A. They were transferred to the credit of Maurice P. Koch, because the checks originally came in in the name issued by Farilla, and that is the way they were entered in the cash receipts book, while they were actually monies borrowed by Maurice P. Koch and contributed to the fund.

Q. That was the \$15,000?

A. That was the \$15,000.

Q. Did that constitute any part of the \$75,000 loss that the partnership took? A. No.

Q. In other words, Mr. Koch's \$15,000 that he borrowed was treated entirely separate?

A. That is correct. [272]

Mr. Fink: That is all.

### Recross-Examination

By Mr. Gillard:

Q. When you say that changes were made, Mrs. Abel, you mean that investment account No. 40 originally corresponded with the original books of entry and showed various items that we have discussed referring to Mr. Frank Farilla, that they were originally entered on Account No. 40 as Frank Farilla, is that correct? A. That is correct.

Q. Then the name Frank Farilla was erased from Account 40?

A. Yes, it is a pencil notation just to break down the account.

Q. In the place of Frank Farilla was the name

(Testimony of Rebecca Koch Abel.)

of Maurice P. Koch?           A. Yes.

Q. Who did that?           A. I did that.

Q. At whose instructions did you do that?

A. On reviewing the account, when checking the records we found this was Mr. Koch's personal investment and not monies due to Farilla.

Q. Where in the records did you find that that was Mr. Koch's money and not Mr. Farilla's?

A. In general discussions, while going through this account.

Q. In other words, it did not appear in the accounts, is that [273] correct?

A. No, it does not appear in the accounts, because the check is entered in the cash receipts under the issuer of the check.

Q. When you just answered me and said in reviewing the accounts you found the error, that was incorrect?

A. We were reviewing the investment account, yes.

Q. There is nothing in the original books of entry show any contribution by Maurice P. Koch individually, is there?

A. No, other than the check from Frank Farilla.

Q. I will repeat the question. There is nothing in the original books of account that show any investment by Maurice P. Koch individually?

A. No.

Q. At whose direction did you erase the words "Frank Farilla" on Account No. 40 in three places and insert the initials "MPK"?

(Testimony of Rebecca Koch Abel.)

A. Well, I couldn't exactly say under whose instructions. I was checking the account to find what constituted this account, and in the breakdown I realized this was not Mr. Farilla's investment, that we were not liable to Mr. Farilla for that amount of money.

Q. You have made the original entries yourself in the cash receipts? A. Yes, I did.

Q. What was there in your review of those entries which indicated that you did not owe that \$15,000 to Frank Farilla? [274]

A. The mere fact that I posted it to the investment account. It would not be in that investment account if we owed that money to Frank Farilla.

Q. Would that be true with reference to Mr. Haller?

A. No, we did not owe that money to Mr. Haller either. That was money that we got——

Q. The checks that were received from Mr. Haller and entered in the cash receipts book were carried under his name in the investment account, were they not? A. Yes, they were.

Q. Why from the accounts themselves did you determine the name Farilla should not be on the investment account as well as on the cash receipts ledger?

Mr. Fink: To which we object at this point on the ground it is purely argumentative.

The Court: She may answer. She made the entry.

A. No, I mean knowing what we owed, if we had



(Testimony of Rebecca Koch Abel.)

owed this amount of money to Mr. Farilla for some time, he would have been hounding us for it, and since he had not, it required investigation.

Q. (By Mr. Gillard): This investment account is not a debt, is it? A. No, it is not a debt.

Q. The fact that his name was on the investment account did not indicate you owed him anything? [275] A. No.

Q. That was not the reason you took Mr. Farilla's name off the investment account No. 40, was it? A. No.

Q. At whose direction did you erase the name, Frank Farilla, and insert the initials "MPK"?

A. We were discussing it. We were going through this and we were told it was Mr. Koch's account.

Q. Who told you that?

A. The partners, when we were discussing this here.

Q. Who in particular?

A. No one. It was in general discussion. I couldn't say exactly who.

Q. Did someone else besides Maurice P. Koch give you that information?

A. There were several of us in the room. I couldn't tell you exactly which one said it.

Q. In other words, the partners had a meeting and agreed that the name Frank Farilla should be erased from the investment account and the initials "MPK," referring to Mr. Koch, should be inserted in place thereof, is that correct?

(Testimony of Rebecca Koch Abel.)

A. They agreed it was Mr. Koch's money coming in and not Mr. Farilla's.

Mr. Gillard: Thank you.

Mr. Fink: Thank you. May we recall Mr. Koch for just a [276] moment.

### MAURICE P. KOCH

recalled as a witness on behalf of the Plaintiffs, having previously duly sworn, testified as follows:

#### Further Redirect Examination

By Mr. Fink:

Q. Mr. Koch, in connection with money used in this picture business, did you have a \$15,000 transaction, or a transaction totaling \$15,000 with Mr. Frank Farilla? A. I did.

Q. What kind of transaction was that?

A. I borrowed \$15,000 from Mr. Farilla to put in this picture deal.

Q. Did you ever repay the money?

A. Yes, sir.

Q. How?

A. I was in business with Mr. Farilla.

Q. You told us that the other day. How did you repay the money to him?

A. When we dissolved the partnership, I accepted that \$15,000 as part of my payment of the business on dissolving the partnership.

Q. In other words, cleaning up your partnership arrangements with Mr. Farilla you accounted for this \$15,000 back to him.

(Testimony of Maurice P. Koch)

A. That is correct, yes, sir.

Q. That is why you cleaned it up? [277]

A. That is correct.

Q. \$15,000 that appears to have been deposited along with the other picture funds, did that come first to Mr. Farilla by way of check?

A. Mr. Farilla gave me the checks and I think there were about two or three checks, and they were turned over—they were endorsed and turned over to the firm, and that is how the name of Farilla got into our books.

Q. When you discovered that later were the books changed? A. Why, certainly.

Q. By the way, the \$15,000 that you are now talking about, was that used for the picture business purposes in 1947?

A. That \$15,000—we were hard pressed for money. The firm of H. Koch & Sons were hard pressed for money. We had a lot of money in the picture business there, and the loan that I obtained from F. Farilla & Sons reduced the loan that we had given Beacon Pictures Corporation by \$15,000, and the firm used that money. That is why our investment was reduced to \$75,000 instead of \$90,000, by me borrowing \$15,000 from Farilla.

Q. Then that \$15,000, you lost that yourself?

A. That is true.

Mr. Fink: That is all.

(Testimony of Maurice P. Koch)

Cross-Examination

By Mr. Gillard:

Q. The original monies that you paid out in this case, the first monies that you paid out, you [278] have testified to—these two checks which total \$17,500—were advanced in the month of May, 1946, is that correct?

A. The first checks that were paid out were \$17,500. I do not remember the exact date. You have the record there, sir.

Q. Exhibit 6 for \$15,000 on April 25th.

A. That is what it says.

Q. Exhibit 8 for \$2,500 on May 22nd.

A. That is what it says there, yes.

Q. The first check that you got from Mr. Frank Farilla was in the month of June, 1946, for \$2,500, is that correct? A. Yes, sir.

Q. At that time had you asked him for \$15,000?

A. Yes, sir.

Q. You had asked him for 15,000 at that time?

A. Yes, sir.

Q. He did not have it?

A. That is right, sir.

Q. So \$15,000 was not borrowed in June, 1956, was it, Mr. Koch?

A. The \$15,000 that I asked him for was going to be given to me in various checks.

Q. So that by June, 1946, you had borrowed from Mr. Frank Farilla, according to your testimony, \$2,500.

(Testimony of Maurice P. Koch)

A. Whatever the record shows there.

Q. That is because you needed the money in the business, you were short of cash, is that [279] correct?

A. That is correct.

Q. The next time you borrowed some money from Mr. Frank Farilla was \$7,500 in the month of October, is that correct?

A. That is part of the \$15,000.

Q. You borrowed \$17,500 from him in October, 1946?

A. Whatever the record shows, yes, sir.

Q. At that time the business was likewise very short of cash, is that correct? I believe your sister testified at the end of October there was an overdraft of \$14.00 in the bank, is that correct?

A. That is what the record shows, yes, sir.

Q. In December, 1946, you borrowed an additional \$5,000 from Mr. Frank Farilla?

A. That was the balance of \$15,000, yes, sir.

Q. In December, 1946, you likewise had an overdraft in the bank, is that correct?

A. That is right, sir.

Q. The final check that was sent to Beacon Pictures Corporation, the \$30,000 check, was in the month of October, 1946?

A. That is right.

Q. Mr. Koch, who instructed that any of your borrowings from Frank Farilla be entered in the investment account No. 40?

A. Originally I did not instruct—I put the money into the firm, I loaned the money, I borrowed the money from Frank [280] Farilla to put

(Testimony of Maurice P. Koch)

in this picture. It was put through the books, and I am not too familiar with the books. I am not familiar how the transaction got in there. I didn't instruct anybody to put it in 40.

Q. It was a borrowing of money from Frank Farilla, was it not?

A. I borrowed the money personally from Frank Farilla.

Q. Personally? A. That is right.

Q. It was not a borrowing of H. Koch & Sons?

A. That is correct.

Q. Who instructed that the transaction be entered in the partnership books of H. Koch & Sons?

A. I deposited the money into H. Koch & Sons.

Q. The Frank Farilla check?

A. Yes.

Q. And that was a debt owed to Mr. Frank Farilla? A. Yes.

Q. Each one of those checks is debt owed to Frank Farilla?

A. I owed it to him personally, not the business.

Mr. Gillard: Thank you, sir. That is all.

Mr. Fink: We have no further questions. The plaintiff will rest, Your Honor.

Mr. Morgenstein: At this time, Your Honor, the defendant would like to make certain motions.

The Court: Does the defendant rest? [281]

Mr. Morgenstein: May we approach the bench?

The Court: I would like to know if the defendant rests.

Mr. Morgenstein: We would like to make our

motion prior to the submission of the case. We would like to submit certain motions to the Court out of the presence of the jury at the conclusion of the plaintiffs' case.

The Court: We are about to take a recess at this time.

(Thereupon the jurors were excused, and in their absence the following occurred:)

Mr. Morgenstein: If the Court please, the defendant would like to move to dismiss and also for a directed verdict pursuant to Rule 50. Our motion to dismiss is based upon the fact that the complaint, the facts and the law fail to sustain a claim for relief, and also the motion for a directed verdict is based upon the fact that the allegations as contained in the complaint are insufficient to prove that the plaintiffs were engaged in the business within the meaning of the term in the Revenue Code and also the facts and the law as presented in this case are insufficient to warrant a jury finding that plaintiffs were engaged in a business as interpreted by the Internal Revenue Code of 1939.

(The motions were argued. During the course of the argument Mr. Gillard made this additional motion:)

Mr. Gillard: If the Court please, may I conclude one phase of this matter which Mr. Morgenstein did not touch upon, [282] and really prior to making the last motion we should have, and I now move the Court for permission to amend paragraph 2 of the

11th count of the answer and paragraph 2 of the 13th count of the answer. Those two paragraphs relate to paragraphs of similar number in the same and similar count numbers in the complaint. Referring to the complaint, paragraph 2, the 11th count, it is alleged, "In addition plaintiff, Maurice P. Koch, advanced in behalf of Beacon Pictures Corporation \$15,000 from the community funds of his wife and himself upon the same basis that the aforementioned \$75,000 was advanced. Said \$15,000 was also lost in 1947."

The answer, which was drawn in Washington prior to the receipt of the administrative files in this office, and prior to any pretrial work, says with respect to that allegation, "Admits, except to deny that this transaction was other than a loan, and except to deny that the basis of this loan was the same as the basis of the \$75,000 loan."

There is a similar allegation in paragraph 2 of count 13, which is the cause of action on behalf of Mr. Koch's wife, Daisy Koch, and the answer of the Government is the same. We request the Court for permission to withdraw that answer and to substitute in lieu thereof the following:

"Denies all the allegations contained in said paragraph."

The reason for the motion is that we believe the evidence [283] as adduced and as produced by the plaintiffs shows that Maurice P. Koch did not advance any personal monies which were involved in this transaction. He did not advance any money to Beacon Pictures Corporation, and he did not lose



any money. The testimony is, as the Court will recall—and it came out just this afternoon for the first time—that these monies that were advanced, the first \$17,500 which was advanced was the money of H. Koch & Sons. Thereafter, because of the financial stress of H. Koch & Sons, Maurice Koch went to Mr. Farilla and borrowed \$15,000 over a period of several months. The last of those borrowings were specifically in accordance with the testimony of the witness because the corporation did not have the money and could not pay. The last one in December, 1946, was subsequent, and all payments had been made for or on behalf of Beacon Pictures Corporation. Merely by entering those borrowings into the investment account the Beacon Pictures Corporation cannot transmute the loan that was made by H. Koch & Sons from that partnership to Mr. Koch individually.

Secondly, the testimony is clear, as Mr. Morgenstein has just indicated, that the loans were made to Sebastian and Hersh and not to Beacon Pictures Corporation.

Third, the evidence is clear that there is no evidence that the money was lost. There was no demand ever made on Sebastian or Hersh for the collection of that money. Therefore we move that we be permitted to withdraw the answer and amend [284] as we have requested to be consistent with the evidence produced by the plaintiffs herein.

(Motions discussed further.)

(At the conclusion of all argument the Court made the following ruling:)

The Court: The motion of the Government to amend counts 11 and 13 of the answer may be denied.

The motion for a directed verdict against the plaintiff, Maurice Koch, individually may be granted, and the motion for a directed verdict as to the remainder—and I am speaking, when I say Maurice Koch, I am speaking of the \$15,000 alone at the moment. As to his interest as plaintiff in the remainder of the thing the motion is not granted, and the motion for a directed verdict as to all of the plaintiffs generally as to the \$75,000 involved may be denied.

The motion is denied under subdivision b of Rule 50.

Mr. Gillard: So the record may be clear, Your Honor, that \$15,000 was divided between Maurice P. Koch and his wife, Daisy Koch.

The Court: Then as far as the \$15,000 is concerned, as it applied to Maurice Koch and Daisy Koch, his wife, the motion for a directed verdict as to that amount and those persons named in that account may be granted. I would like to see counsel in chambers as to the instructions.

Mr. Fink: I was wondering if we might not require certain [285] stipulations at this point, in view of the nature of the special interrogatory we are going to submit to the jury.

The Court: I was going to do that in chambers. We can do that here while the reporter is here.

Mr. Gillard: Prior to that time, if Your Honor please, the Government will rest its case.

The Court: May it be stipulated by both parties that in view of the Court's rulings up to this time, that the only issue to be presented to the jury is the special interrogatory which reads as follows:

"During the year 1947 was H. Koch & Sons regularly engaged in the business of financing motion picture ventures? Yes—no."

May that be stipulated?

Mr. Fink: So stipulated.

Mr. Gillard: So stipulated.

The Court: May it be further stipulated that thereafter, after such special interrogatory has been submitted to the jury, that all motions, issues and facts involved in the case are to be determined by the Court unless the parties stipulate as to such motions, issues or facts?

Mr. Fink: So stipulated.

Mr. Gillard: So stipulated.

The Court: Are there any further stipulations that are required? [286]

Mr. Fink: I do not believe so, Your Honor.

The Court: I would like to see counsel in chambers.

(Counsel for the respective parties then adjourned with the Court to the Court's [287] chambers.)

Thursday, November 29, 1956

(The following proceedings were had in the Court's chambers, there being present the Court, counsel for the respective parties, the reporter, but no jurors being present:)

Mr. Fink: We are all assembled here now. The record may so show.

Comes now the plaintiffs and each of them and moves this Court for a directed verdict in favor of the plaintiffs; in the alternative, that the jury be instructed to return a "Yes" answer to the interrogatories being propounded to them pursuant to the stipulation.

Said motion is made upon the grounds as follows:

First, that the parties plaintiff to this action heretofore, and on the 23rd day of October, 1944, entered into a solemn contract between themselves which reads, among other things, as follows.

And I turn to paragraph 1 of Exhibit 2:

"The said partnership business will, in addition to engaging in those activities referred to in the existing partnership agreement, engage in the business of financing motion picture productions either by direct participation in such productions by way of stock investments or loans to motion picture producers or in any other form of financing that said partners [288] may mutually agree upon between themselves. It being understood in this connection that the said partnership may carry on such business as aforementioned either as joint adventures

in association with others, strangers to this partnership, or with any other person, firm or corporation the said partners deem advisable.”

To hold in this case that the partners, after their solemn contract as between themselves, and which gives the only right for taxation that the Government may have, to hold in effect in any manner, shape or form these partners are not engaged in the manufacture of motion pictures when they have by their solemn contract so contracted to do would breach the form of contract and be contrary to the position contended for by the defendant.

Secondly, since there is no evidence in this case sufficient upon which reasonable men could possibly find that the plaintiffs were not engaged in the business of motion picture financing, both under the terms of their solemn contract as well as under the facts of this case.

In this regard it is our position that the parties having contracted between themselves to engage in the business of motion picture financing have, first of all, be foreclosed from their inquiry into that subject by the taxing authorities.

Secondly, that the facts in this case tend in every respect and only to establish that they did so engage pursuant to their agreement so to do. [289]

The Court: The matter may be submitted?

Mr. Fink: Yes, Your Honor.

The Court: The motion may be denied.

(Thereupon the Court convened in the courtroom, and in the presence of the Court, the

jury, and counsel for the respective parties, counsel made their closing statements to the jury, at the conclusion of which the Court instructed the jury as follows:)

The Court: It now becomes the duty of the Court to instruct the jury upon all questions of law. It is your duty to follow the instructions of the Court and to accept the law as given you by the Court. You are, however, the sole and exclusive judges of all questions of fact and of the weight and effect of the evidence and of the credibility of the witnesses. Your power of judging the effect of the evidence, however, is not arbitrary but is to be exercised with legal discretion and in accordance with the rules of evidence.

You are not to consider for any purpose any evidence which has by the order of the Court been stricken out, or the offer of any evidence which has not been admitted by the Court.

The statements and the arguments of counsel, and any purported statement of fact contained in any question asked by any counsel of any witness are not evidence in the case, and any statements made by a counsel either during the trial or during the argument, which are not supported by the [290] evidence, or which are inconsistent with my instructions as to the law, are to be disregarded by you. This, however, does not apply to stipulations of fact by counsel, which stipulations of fact must be treated by you as facts proven in the case.

In these instructions the Court is expressing no

opinion upon any of the issues required to be determined by the jury.

All principles of law given in these instructions are of equal importance. In civil cases, which this is, the affirmative of the issue must be proven by a preponderance of the evidence. The affirmative here is upon the plaintiff as to all of the affirmative allegations of the complaint which have not been admitted by the answer. If the evidence is contradictory, your decision must be in accordance with the preponderance thereof. When the evidence in your judgment is so equally balanced in weight and quality, effect and value that the scales of proof hang evenly, your verdict should be against the party upon whom rests the burden of proof.

This is an action brought against the United States Government by three brothers and a sister, to wit, Harold M. Koch, William L. Koch, Maurice P. Koch and Rebecca Koch Abel, together with the wives of the three brothers, for the refund of income taxes paid while the three brothers and the sister were members of a partnership known as H. Koch & Sons. The years for which the refund is claimed were the years 1947 and 1945. During those years the partnership of H. Koch & Sons [291] filed an income tax return and the individual partners paid taxes thereon. Later in 1949 the partners and their respective wives, who are the plaintiffs in this action, filed an amended income tax return for the year 1947, and later filed a claim for a refund with the Commissioner of Internal Revenue, contending that there had been a business loss in

the business of the partnership for the year 1947, and that inasmuch as this loss was greater than the income for 1947, that they were entitled to use the amount of the loss in excess of the income for that year to offset any gain in the prior year of 1945.

Thereafter the Commissioner of Internal Revenue made a determination that the loss incurred by H. Koch & Sons was not as a result of a business bad debt but that the loss occurred by reason of a non-business bad debt.

Thereafter plaintiffs filed this action against the United States, and in that complaint affirmatively alleged that the loss incurred by the plaintiff was one incurred while H. Koch & Sons was regularly engaged in the business of financing motion picture ventures.

The complaint alleges that the Collector of Internal Revenue notified the plaintiffs that in his opinion the loss in question was a non-business bad debt and refused to allow the full deduction claimed by the plaintiffs.

It is admitted in this case that H. Koch & Sons is a copartnership consisting of Rebecca Koch Abel, Maurice P. Koch, [292] Harold M. Koch and William L. Koch. It is conceded by the Government that the partnership did suffer a loss through the year 1947 in the amount of approximately \$75,000 in connection with a certain motion picture venture. However, under the provisions of the income tax law the entire amount of this loss can be deducted



in the years 1947 and in 1945 only if it was the type of loss which permits such a deduction.

The plaintiffs in their complaint allege that the loss was either a business bad debt, a loss incurred in the business of producing motion pictures or a joint venture in the business of producing a motion picture, to wit, "Copacabana," and that in any case it constituted a loss from a business regularly carried on by H. Koch & Sons.

The Government, on the other hand, contends that the loss incurred was not one which was incurred in the trade or business regularly carried on by the plaintiffs, but that it did result by reason of a non-business bad debt. The law provides that if a non-business debt becomes worthless within a taxable year, the loss resulting therefrom shall be considered a loss from the sale or exchange of a capital asset, and that the treatment for income tax purposes of that loss would differ, depending upon whether H. Koch & Sons was regularly engaged in 1947 in the business of financing motion picture ventures.

The law provides that the taxpayer gets certain credit over a period of years upon his income tax return by reason of [293] the loss of a capital asset, but those credits do not permit him to take the full loss by offsetting that loss against the business income for the particular years in question, unless the loss resulted from a business regularly carried on by the taxpayer.

The question here to be determined is whether H. Koch & Sons were in 1947 regularly engaged in the

business of financing motion picture ventures. In determining that question you should consider all of the evidence which has been admitted in the case. The question of whether the debt is one the loss from the worthlessness of which is incurred in the taxpayer's trade or business is a question of fact in each particular case. The statute does not give a definition for the word "business." Accordingly, in determining whether H. Koch & Sons was regularly engaged in the business of financing motion picture ventures you should consider the word "business" to have its ordinary, common and accepted meaning. A taxpayer may engage in or regularly conduct one or several businesses at the same time. The amount of time as well as the proportionate amount of capital devoted to a particular business are each factors among other factors to be considered in determining whether or not one is regularly engaged in a particular business.

If a taxpayer regularly and continuously participates in business ventures in which he is not only financially interested but to which he devotes a substantial part of his time, such [294] activities may make such ventures a trade or business of the taxpayer. Isolated or infrequent transactions of a taxpayer in any field do not constitute a trade or business within the meaning of the Internal Revenue Code.

In determining whether an activity of a taxpayer is a trade or business you should consider among other things how extensive was the activity, the financial investment therein, whether it was regu-

larly carried on, and whether the activity occupied a substantial portion of the time, energy and effort of the taxpayer.

Taxpayers may act through employees, agents and other persons, firms and corporations appointed by such taxpayers, and the acts of such employees, agents or other persons, firms or corporations appointed by the taxpayer are in contemplation of law the acts of the taxpayer. Thus in considering the activities of the taxpayers in the instant case with relationship to the conduct, if any, of the business or enterprise, you are required to consider that the acts of any such employees, agents, persons, firms or corporations appointed by them are in fact the acts and the activities of the taxpayers.

The authorized act or acts of any one partner of H. Koch & Sons in connection with the partnership business or activities are in contemplation of law the act or acts and activities of all the [295] partners.

The burden of proof in this case is upon the plaintiffs to prove by a preponderance of evidence that the loan by plaintiffs to the Beacon Pictures Corporation was a loan made in plaintiffs' regular trade or business. There is a presumption that the determination by the Commissioner of Internal Revenue that the plaintiffs were not engaged in the trade or business of financing motion pictures is correct. The burden is upon the plaintiff to overcome the presumption of the correctness of the Commissioner's determination by proving by a preponderance of evidence that they were engaged in

the trade or business of financing motion pictures.

By a preponderance of evidence is meant such evidence as when weighed with that opposed to it has more convincing force, and from which it results that the greater probability is in favor of the party upon which the burden rests. Preponderance of evidence means not the greater number of witnesses but the greater weight, probability, quality and a convincing effect of the evidence and proof offered by the party holding the affirmative as compared with any opposing evidence. If the scales of proof hang evenly the verdict should be against the party who has the burden of proof.

In determining whether any issue has been proven by a preponderance of evidence you should consider all of the evidence bearing either way upon the question, regardless of who produced it. A party is entitled to the same benefit from [296] evidence that favors his cause or defense when produced by his adversary as when produced by himself.

If you believe that Maurice P. Koch used his own money in any transaction and was acting therein in his own behalf and not on behalf of H. Koch & Sons, that transaction cannot be considered by you in determining whether the partnership of H. Koch & Sons was engaged in the business of financing motion picture ventures.

The jury are the sole and exclusive judges of the effect and value of the evidence addressed to them and of the credibility of the witnesses who have testified in the case. There are a few standards or rules by which you can measure the testimony of

the witness and evaluate it and determine whether or not you want to believe it or how much of it you want to believe. The character of the witnesses as shown by the evidence should be taken into consideration for the purpose of determining their credibility, whether or not they have spoken the truth. The jury may scrutinize the manner of the witnesses while on the stand and may consider their relation to the case, if any, and also their degree of intelligence.

A witness is presumed to speak the truth. This presumption, however, may be repelled by the manner in which he testifies, by his interest in the case, if any, or by his bias or prejudice, if any, or by contradictory evidence.

A witness may be impeached by contradictory evidence or by [297] evidence that on some former occasions he made statements or conducted himself in a manner inconsistent with the present testimony as to any matter material to the cause on trial.

A witness wilfully false in one part of his testimony is to be distrusted in other parts. The jury may reject the whole of the testimony of a witness who has wilfully sworn falsely as to a material point. If you are convinced that a witness has stated what was untrue as to a material point, not as a result of a mistake or inadvertence, but wilfully and with a design to deceive, then you may treat all of his testimony with distrust and suspicion and may reject it all, unless you shall be convinced that he has in other particulars sworn to the truth.

You may also consider the manner in which a witness may be affected by the results of your verdict. You may also consider the extent to which he may be corroborated or contradicted by other evidence and, of course, finally any matter in general which you contend reasonably sheds light upon the credibility of the witness may be considered by you.

You must weigh and consider this case without regard to sympathy, prejudice or passion for or against either party to the action. Your verdict is to be reached upon the evidence produced upon the trial of this case, and you will not permit speculation, conjecture or sentiment to influence you one way or the other. [298]

A corporation is an artificial person. It must necessarily act through its servants, agents and employees. An act of an employee within the scope of his employment is the act of his employer. This case should be considered by the jury the same as if it were an action between persons of equal standing in the community. The fact that the defendant is the United States should not affect or prejudice your minds in any way, but the rights of the parties should be determined upon the evidence introduced in the case and the instructions given to the jury, which is the law and the only law to guide you in your deliberations.

The computation of income taxes is a complicated process and it is a very difficult matter to determine the exact amount which may be due. As I have stated, it is the function of the jurors to determine questions of fact. The question of fact in this case

is whether in 1947 the partnership of H. Koch & Sons was regularly engaged in the business of financing motion picture ventures. Accordingly, counsel on both sides have agreed upon a procedure which will simplify your labors in this case. It has been agreed that there will be submitted to the jury a certain question, and the jurors are merely to determine whether its answer to that question is in the affirmative or in the negative. The plaintiffs contend that your answer to that question should be in the affirmative. The defendant contends that your answer to that question should be in the [299] negative. When the question is answered, certain legal conclusions follow therefrom which will be determined by the Court, and the proper amount of income tax to be paid by the plaintiffs for the years 1947 and 1945 will be ascertained.

It is your duty as jurors to consult with one another and to deliberate with a view of reaching a verdict if you can do so without violence to your individual judgment. To each of you I say you must decide the case for yourself, but you should do so only after a consideration of the case with your fellow jurors, and you should not hesitate to change an opinion when convinced that it is erroneous. However, none of you should vote for either side nor be influenced in so voting for the single reason that the majority of the jurors are in favor of such party. In other words, you should not surrender your honest convictions concerning the effect or weight of the evidence for the mere purpose of returning a verdict, or solely because of the opinion

of the other jurors. Your verdict in this case, of course, must be unanimous.

Counsel, I am about to conclude my instructions. Is there any matter you desire to take up in the absence of the jury?

Mr. Gillard: Yes, your Honor.

Mr. Fink: No, your Honor.

The Court: There has been prepared for your convenience, as I have indicated, a special verdict. Omitting the title of the court and cause, this special verdict reads as follows: [300]

“During the year 1947 was H. Koch & Sons regularly engaged in the business of financing motion picture ventures?”

Answer, with a blank line, and then a blank line for the signature of the foreman.

If your answer to that question is “Yes,” your foreman will write the word “Yes” in the blank space provided and will sign the verdict to which you have agreed. If your answer to that question is “No,” the foreman will write the word “No” in the blank space and will sign the verdict at the place indicated.

If you desire to see any of the exhibits that have been introduced in evidence, if you will advise the Court officer, they will be delivered to you to the jury room.

Upon retiring to the jury room you will select one of your number to act as foreman. This foreman will preside over your deliberations, will sign the verdict to which you may agree, and will represent you in any future proceedings in the courtroom.



The person so selected should permit a full and fair discussion of the case, and the other jurors should assist the foreman in keeping the proceedings orderly and in expediting the proceedings in the jury room.

You may now retire and deliberate upon your verdict.

Mr. Gillard: If your Honor please, in response to your question we said yes, we did have some matters we would like to take up in the absence of the jury. [301]

The Court: Mr. Gillard, I asked you and I heard no answer and I went on.

Mr. Gillard: I said, "Yes, your Honor, we do." I am sorry.

The Court: I beg your pardon. I did not hear you.

(Thereupon, the Court and counsel for the respective parties adjourned to the Court's chambers, and in the absence of the jury the following took place.)

Mr. Gillard: If your Honor please, we would like to take exception to certain of the instructions given and certain of the instructions proposed by the Government which were not given.

We take exception to those portions of the charge given as follows: That portion which stated that the jurors are to consider all the evidence submitted in the case. We take exception on the ground that this is erroneous, that much of the evidence relates to conduct of the corporation and officers of the cor-

poration which we feel is not attributable to the partnership.

If your Honor please, we take exception to that portion of the charge which states to the jury the term "business" in the Internal Revenue Code is to be considered as having its ordinary meaning. We feel this is an erroneous application of the law as stated by the Supreme Court, and allows the jurors to consider facts which should not be considered in determining [302] the meaning of the word "business."

We also take exception to that portion of the charge which states that taxpayers may act through agents and corporations, and those acts of those agents and the corporations are to be considered as the acts of the taxpayers themselves. We feel as applied to this case, your Honor, this is an erroneous statement of the law as applied to the facts, in view of the fact that most of the activity was done by the corporations themselves, and since the issue in this case is whether H. Koch & Sons was a partnership regularly engaged in the business, the acts of the corporation in which the partners are officers, stockholders or members should not be considered as the acts and conduct of the partnership itself.

We also take exception, your Honor, to the failure to give certain charges requested by the defendant and those are as follows:

The defendants requested Instruction No. 5, to the effect that investing and financing is not a trade or business and should not be considered as a trade or business. We feel the failure to give—

The Court: The instruction is set out. It will be filed, so the record will show what 5 is.

Mr. Gillard: We feel the failure to give this instruction results in prejudice to the defendant, in that in relation to the other instructions given it allows the jury to consider as [303] evidence the financial activities, activity which cannot be considered a trade or business within the meaning of the Internal Revenue Code.

We also take exception to your Honor's failure to give Charge No. 6, proposed Charge No. 6, to the effect that—or your modification of Charge 6, that the activity may be a substantial portion instead of a major portion. We feel that the proposed instruction is a proper statement of the law, and that as given to the jurors in relation to the entire charge will allow the jurors to determine that a trade or business did exist when no such trade or business could exist within the meaning of the Internal Revenue Code.

We also take exception to the failure of your Honor to give Defendant's proposed Instruction No. 7, which relates to the fact that a partnership, that the mere fact that a partnership was formed does not mean the taxpayers are engaged in a trade or business. We feel a failure to give this charge in relation to the other instructions given to the jury results in the jurors being able to determine that a trade or business was regularly carried on merely by looking to the existence of a partnership agreement. We feel this is not the law, and in re-

lation to the entire charge any such finding by the jurors would be erroneous.

If your Honor please, we take exception to the Court's failure to give Charge 8 as requested by the defendant to the [304] effect that the business carried on by the corporation is not the business carried on by shareholders and directors. We feel the charge proposed by the defendant is a proper statement of the law, and in the situation and facts presented to this jury the jurors are now able to determine that the acts of the officers while carrying on corporate activity are the acts of H. Koch & Sons, the partnership itself. We feel that such is not the law, and such an instruction, when failed to be given in relation to the other instructions, is clearly erroneous and results in prejudice to the defendant.

We also except your Honor's failure to give Charge No. 9 as proposed by the defendant, to the effect that the activity of Maurice P. Koch as shareholder, officer and director of Producers Finance Corporation cannot be considered the activity of H. Koch & Sons. We feel that the instruction as proposed by the defendant is proper, and by failing to give this instruction in relation to the other charge results in prejudice to the defendant, in that the activity of Maurice P. Koch as a corporate officer may now be considered by the jurors as the activity of H. Koch & Sons in determining whether or not H. Koch & Sons was engaged in a trade or business.

If your Honor please, we also take exception to the Court's failure to give defendant's proposed in-

struction appearing on the first page of the supplemental instructions, to the effect that the jurors are instructed that an income [305] tax deduction is a matter of legislative grace. We feel the failure to give——

The Court: Don't repeat the same statement, counsel, which you do after each instruction. When you make your objection then make a general statement if you wish, but you have been repeating the same one after every instruction.

Mr. Gillard: There have been certain modifications. However, in this charge we feel there is not sufficient weight given to the internal revenue laws of the United States.

Mr. Fink: May we, in view of the exceptions taken, have the exceptions of the plaintiff at this time? The plaintiff excepts to the failure of the Court to give Instruction No. 13, instructing the jury that the jury may consider in determining whether or not H. Koch & Sons is engaged in the business of financing motion picture ventures the amount of time and effort expended in that direction, whether or not actual ventures were concluded.

In addition, we respectfully except to Instruction No. 15 to the effect that in considering the question of whether or not H. Koch & Sons devoted a substantial time to the financing of motion picture ventures the jury is required to consider all of their activities relating to that purpose of whether or not actual financing was concluded.

We also except with respect to the instruction given by the Court that the jury may disregard all

the activities of [306] Maurice Koch if such activities involve only him, his own funds, having been particularly held by this Court that as a matter of law all of Maurice Koch's activities in the motion picture business, the business of financing motion picture ventures were for and on behalf of the partnership rather than his own behalf and a motion having been granted by reason thereof.

The Court: Very well.

(Thereupon, the Court and counsel returns to the courtroom, and in the presence of the jury the following occurred.)

The Court: The formalities have now been completed and you may now retire to deliberate upon your verdict. You may now retire.

(Thereupon, at 1:45 p.m. the jury retired to deliberate upon its verdict.)

The Court: May it be stipulated, gentlemen, in the event the jurors desire to see the exhibits in the case that they may be delivered to the jury by the Court officer without further order of the Court?

Mr. Fink: So stipulated.

Mr. Gillard: So stipulated.

(Thereupon, at 5:35 p.m. the jury returned to the courtroom and the following occurred.)

The Court: Let the record show the jury is present. Ladies and gentlemen, have you agreed upon a verdict?

The Foreman: We have. [307]

The Court: Mr. Phipps, you are the foreman, are you?

The Foreman: Yes, sir.

The Court: Hand the verdict to the Court officer, please. Mr. Clerk, omitting the title of the court and cause, will you read the special verdict and ascertain whether that is their verdict?

The Clerk: Ladies and gentlemen of the jury, listen to your verdict as you have rendered it:

During the year 1947 was H. Koch & Sons regularly engaged in the business of financing motion picture ventures?

Answer: No. Signed "Charles L. Phipps, Foreman."

Is that your verdict as rendered?

(All members of the jury indicated in the affirmative.)

Mr. Fink: If the Court please, may we poll the jury?

The Court: Mr. Clerk, poll the jury. Ladies and gentlemen, as your names are called, if your verdict was as read by the Clerk, please answer "Yes."

(The jury was polled, each juror answering in the affirmative.)

The Court: The verdict may be recorded.

Ladies and gentlemen, thank you very much for your service in this case. You are excused from further attendance, and the Clerk's Office will notify you when you are required to appear again. You may now retire.

Mr. Fink: The plaintiff hereby moves the Court for judgment [308] notwithstanding the verdict. I do not know whether your Honor wants to take that matter up at this time. More appropriately it can be taken up at some other time.

The Court: Just as you please, counsel. By reason of the fact that you are from out of town I would make the hearing of that at your convenience.

Mr. Fink: Perhaps we could have the hearing sometime tomorrow at your Honor's convenience?

The Court: Very well, ten-thirty tomorrow morning. [309]

November 30, 1956, 10:30 A.M.

Mr. Fink: If the Court please, come now the plaintiffs, in order to clarify our motion, and move for a judgment notwithstanding the verdict and a judgment in favor of the plaintiffs and each of them, and likewise move that the special finding of the jury be vacated, set aside, and judgment entered for the plaintiffs notwithstanding such special finding. We take the law to be that a motion for a new trial at this particular juncture in this special type of proceeding would be premature insofar as the plaintiffs are concerned, in that judgment has not been entered, and the plaintiffs reserve the right to move for a new trial at a subsequent time after the entry of judgment in this cause. On the other hand, we assume the state of the law to be that the Court may at any time on its own motion grant a new



trial, that is, at any time up to a period of ten days following the entry of judgment.

(The motions were argued by both counsel, at the conclusion of which the following occurred:)

The Court: This motion may be submitted. I take it there are two motions here, a motion for a judgment notwithstanding the verdict and a motion that the special verdict be set aside.

Mr. Fink: Yes. I think we could clarify the record by taking one further step, and that is, neither side has any further evidence to offer in this case. [310]

Mr. Gillard: That is true. The matter was submitted.

The Court: It may be stipulated by both sides there is no further evidence in the case to be submitted.

Mr. Fink: Prior to judgment, yes.

The Court: Is that right?

Mr. Gillard: That is correct, your Honor.

The Court: The matter at this time may be submitted. [310-A]

November 29, 1956

The Court: The jury are present. Proceed.

Opening Argument to the Jury  
On Behalf of the Plaintiff

Mr. Fink: If it please the Court, counsel, ladies and gentlemen of the jury, there may be certain facets of this case, due to the limited function the jury will play in this case, that are somewhat confusing at this time, but I believe we can relax because I believe when the discussions by counsel and the instructions of the Court have been given to you, this case will be a very clear and simple one for you to decide.

First of all, I would like to tell you the story about the law suit. H. Koch & Sons, a partnership, admittedly, consisting of four people we have talked about, three brothers and a sister, made their tax return for the year 1947, reported their income and paid their taxes. There is no question about that. Later on, due to the fact that the picture business, as you have been told and as you know goes on throughout the world, they found out in 1947 a certain film that they had money in went dead and the thing was a total loss. So they amended their tax return, filed their amended tax return, which is in evidence here, and they asked for a refund of their tax money. These papers were with the various Government agencies over a period of some years and it was finally turned down, so they brought the law suit to get back the taxes they paid.

A law suit is always made up, first of all, of a complaint. You file your law suit and tell your story about what you complain and circumstances that surround it. In this case the pleadings, which were the complaint and the answer, the complaint showed that H. Koch & Sons is a partnership, that in the year 1947, which is our year in question, they sustained a loss by reason of certain funds they advanced and became lost in that year, and that as a result, instead of having paid taxes, they were entitled to a refund, each one of them for the taxes paid.

Then the answer to the case can either admit everything that they said or can deny it, or it can admit part and deny part. In this case the answer, I believe prepared by somebody back in Washington, was filed in this case and says, "Yes, we admit you were a partnership. We admit you paid your taxes. We admit you put some money into some pictures. We admit you lost your money. We admit everything, except we say but—" This answer says—"but, although you are ordinarily entitled to deduct your losses, in this particular case the loss which you have incurred here is a non-business bad debt. It is not proximately related to your business, and therefore because it is a non-business bad debt—" that is the "but" of this particular answer—"we are not going to allow it." [2\*]

So the question arises, was the debt incurred in a business or was it a non-business bad debt? Of course, I know that you all agree under our de-

mocracy anyone who claims they have something coming has a right to come to court and bring their lawsuit. He has the right to have the case tried before a jury of their neighbors in this community. I know that you realize also just because someone claims, files a lawsuit and makes a claim does not mean they are entitled to collect or entitled to win, and by the same token I know you also know because somebody denies your claim, a part of it, does not mean that they have any good defense.

This case, as we have mentioned, gets down to only a single question. I know that some of you tried cases before. In most cases it was a matter perhaps involving how many dollars and cents should the jury give, but in this case that is not present because we all agree we followed the tax tables in determining how much the plaintiff is entitled to. There is only one question left open in this case and that is, was this a non-business bad debt or was it a loss incurred in a business regularly conducted? And all of the testimony in this case which does not bear on that issue, so far as we are concerned, is no longer important, because all you are going to be called upon to answer, I believe—right now I do not know what the Court will instruct you, but I believe all the Court will tell you is that all you have to answer is yes or [3] no to the one single question that will be propounded to you, and that is going to be the limited function of the jury in this case. That is the only question open in the case really and that is whether H. Koch & Sons was engaged in the business of financing motion

picture ventures. It is as simple as that. You will answer yes or no and this case is over.

We talk about a business, and I think when you come to court you do not leave your common sense home. The word "business" here, I believe the Court will tell you, means the same as the word we use up and down the streets, in our homes and in the market place. The word means just that—business. It has no peculiar meaning, any different in the court room than it has in your ordinary life. However, I believe it would be well to examine what this business here consisted of.

To begin with, as I said, I don't know exactly what the Court will instruct you, but I believe the Court will tell you this, that any person or any firm can engage in any number of businesses. In other words, you can have a big business and you can have a teeny one, or you can have a dozen small ones. I know Miss Ernst and Miss Nordlund will tell you the Standard Oil Company have all kind of businesses. They are in the oil business, but they have other kinds of businesses, too. H. Koch & Sons is not any Standard Oil Company, but they certainly have the right to be, as the Court will tell you, in as many businesses as they want to be in. It doesn't [4] matter that they were in more than one business. They could be in any number they wanted to be in.

The Court will also tell you it is altogether possible for a person to have a big business and a small business, a business that they devote the major part of their time to and a business that they devote a

lesser amount of their time to. I think the Court will also tell you that they have a business which they devote their major assets to or their minor assets to. Still both of them are businesses. In this case we are talking about the motion picture business. When we talk about the motion picture business, that is quite different from most businesses. For that matter, I don't think the man who filed the answers in this case knew very much about the motion picture business. This is a business that is built on ideals. You just don't go out and put money in the motion picture business as you put it in stocks and bonds listed on the market. You start out and all you have is an intelligible, fleeting idea. If you take any of those ideas and follow them up, you are going to have an investment of over a million dollars. You have to start out, first of all, and you have to find a property in which you have confidence, a story. That is your foundation. You have to make sure that you acquire the property on the right terms so that you don't ever lose it, so that you can protect it. You are not going to build a 12-story building that cost you a million [5] dollars on a lot you don't own. The same thing is true. You are not going to make a picture based upon a story you do not own.

The next thing you have to have, you have to have, stars and, of course, the Kochs are not glamour people. They are hard-working people. They are not going to act in any pictures. They have to have stars. Not only that, but every picture has more than one star. It takes several stars. If you want stars for your

picture, you have to have them available all at the same time, because if one is making a picture in Europe and someone else is getting a divorce in Reno, you cannot start work. They have to be there when your stars are ready. The same thing is true with the director. We are talking, you know, about the independent motion picture business. This is not M-G-M, Paramount or Twentieth-Century-Fox, where they have the high-priced people under salary and know their backing. These pictures start out with a group of men who have their hands in their pockets and that is all. They have to find a studio that will rent them some space, having stages, cameras, laboratory facilities. They have to hire a complete staff, and all the time they are working on an idea. And, you know, one of the toughest jobs in the world is the creative job of following through on an idea. You get many of them. You follow through on them. You sleep on them by night, wake up with them in the morning, take them to lunch, dinner and [6] breakfast with you. You think about them all day long, and you work with them all day long. It is very intangible, and you have very little to show. What you are really doing, until that camera starts to grind, you are really experimenting, and we all know when you are experimenting you have many experiments that start but very few that end up. They start out in the picture business in some respects similar to the way they start in the oil business. A man goes out and finds the land. He gets together interested people. They get the machinery

to drill the well with. They start out and they hit a dry hole. Because they hit a dry hole does not mean they were not in the oil business. The question, is where did they devote their activities? When you experiment with something as you do with a picture until you get it all together, all packaged—let me tell you something. We have had a number of documents in evidence here. They remind me of the iceberg. They say that only about two per cent of the iceberg you see floating in the ocean is above water and is the part that you can see. Ninety-eight per cent is below the water. You can't even see it. Every one of these papers—they are just about two per cent—they are just the things that we can now see and tangibly bring to you.

But the thinking, the planning, the hoping, the trying to get in to get a star, trying to get a studio, trying to get the important people you have to get in touch with, [7] negotiating with them, getting money together—all these things that you can't see here at all, these just are little things that happened. Obviously you can't sign a contract with a star or a director or have a studio—you prepare all the contracts, but there is no use in committing yourself to use a star on January 1st and pay him \$150,000.00 if you haven't got everything else that goes with it. So the contracts build up. You don't sign them until you have everything together at one time. You don't permit yourself to use a studio when you have nobody to put in that studio. Of course, one of the things you have to have is a release for your picture. You can't make the film and



take it home with you. You can't put it away in a vault. This picture is made for release. You have to have a release throughout the whole world to get your money out of it, some selling organization that operates throughout the world. They are few and far between. So all this talk you have heard here about things that didn't work out, these are the pains, the headaches that are normal and natural to this piece of experimentation and, frankly, I don't believe we had any showing in this courtroom to the contrary.

When you get into the picture business, that is a big piece of business. There is no single group of people who have independently gone out to do feature pictures, who have done too many of them in a lifetime. Each picture deal is a [8] tremendous milestone. It generally requires years to get one completely through. You have many starts, many attempts.

I am reminded of the days when I was much younger. I lived in Oklahoma. We used to live in a very small town. That was a day of the so-called drummer traveling salesman. He used to come up those dirt roads and go from village to village, from town to town and sell his goods. On Saturdays the stores were busy and they couldn't work. They stopped at a small inn that was near and they would get into a conversation. The story is told that one rainy Saturday afternoon one of these drummers said hello to another fellow he didn't know. He said, "How's business?"

He said it wasn't bad. He said, "I sold 200,000 white last week, 150,000 pinks, 100,000 blacks and

100,000 yellows and some reds." He said, "How's business with you?"

The fellow said, "I haven't had a sale in 18 months, not a single sale in 18 months."

The first fellow said, "You haven't had a sale in 18 months? What are you selling?"

He said, "I am selling steel bridges. What are you selling?"

He said, "I am selling jelly beans."

When you get in the picture business, you aren't doing business with jelly beans. You are not selling groceries. You are getting together a tremendous project and hope all [9] the elements of this project will somehow get together, coagulate so that you have a successful picture.

Insofar as the picture business again, I want to mention to you you are not buying something you are going to take home and put away in your vault, like an investment of your savings. You are not buying something for yourself. You are actually making something for resale, which is in itself the business.

I would like to turn for a moment, since we have had a view, first of all, of the general nature of lawsuits and, secondly, what this picture business is about, and I am pretty sure having heard the testimony you heard, you have a pretty good idea about it now, if you did not have before you came here. Let us turn for a moment to the Koch family. I think there is one thing we are all convinced of here, and that is these people are good people. I

don't think anybody can doubt that. They paid their taxes and they lost their money. This is all admitted. There is no question about it. And just thinking about that lawyer's testimony. He was a young lawyer starting out and his wife had to go to the hospital. I am thinking of Pop Koch, the father, gone to his eternal rest. And it reminds me of an ancient story about the old father who had is four children with him. He was going to die and he said to his children, "Bring me sticks." So they brought the sticks. He took one stick and he broke it and tossed it away. He took four sticks and put them together. [10] He couldn't break them. And he said, "See, my children, I want you to know that you are like these four sticks, that together you have strength, separate each of you can be broken."

These four children of Pop Koch have stuck together, one-for-all and all-for-one. They have worked and they have tried. They have tried no doubt and they would have tried anything that would have made them successful. But I know that you know one thing, that these Kochs, one-for-all and all-for-one, that is the only way they are. No other way.

You have had the testimony from the witness stand with the single exception of this friend of Maurice Koch's, who came back from the Army, he and his wife lived at the home three months and he got involved in business with him—that is the single exception in all these years. There has been no business dealings except the partners, and these four children of Pop Koch stuck together. We know the

Koch family were making luggage. Mr. Koch was on the War Production Board. During the war with people being displaced, there was a big demand for luggage, if you could get the material to make it with, but the number of manufacturers just doubled, and their claim was that H. Koch & Sons at that time was a well-known brand but had no particular standing in the trade, just another company making luggage. He knew, and I think it was pretty good foresight, at least he thought that there was going to be tremendous competition and they were all going broke. He [11] thought, "I want to find something else to get into." When these people started to find something else to get into, you must bear in mind the only connections, the only affiliations, the only other business they had any contact with was the motion picture business. They also knew they were not actors, they were not directors. By the way, everybody down in Hollywood is not a glamour face. That is for the actors and actresses. But in the picture business no matter how many actors you have, no matter how many studios you have, how good your story is, no matter how many people you have working for you, you can't make a picture without money. You can't do anything without money, as we all so well know. The picture business comes down to two sides.

One side is called the creative side. That becomes worthless if you don't have the other part. It is like slicing a man's heart in half. Half of it is worthless.

The other side is money. You have to have money on one side; the creative side is the other side.

Money has to have financial management with it because creative people just are not given money without financial management. There is reason for that. A creative man wants to create, wants the greatest achievement of all time to stand as a monument to him for all eternity. The financial man knows he has so much money he has to make a picture with. You have those two elements that make up the picture business. [12]

The Koch family realized they had better start getting into something else just in case. They had Maury scurrying to his friends and associates in Hollywood to get into some picture ventures. As I told you, nobody makes a picture by himself in the independent field. It is always a group. They start and get together with all kinds of people. You heard the story, and I want to tell you again that in between each one of these pieces of paper, in between everything that happened there were days and nights of meetings, there were days and nights of trying to formulate, trying to do, and the Kochs get an A for effort in your book, I know. They went down there and put up all their money, too. This was no taking of some surplus funds and tucking this away in the old sock where it was safe. This was taking all their money and putting it into a business that is the greatest gamble in the world because you are experimenting and you might get a hydrogen bomb out of your experiment, or you might get a dry hole. You might get nothing.

They didn't take surplus money when they were overdrawn in the bank. This was their finances, this

was their cash, this was their money, this was really important. \$50,000.00, \$30,000.00, \$20,000.00, \$25,000.00, Producers Finance Corporation, a million dollars worth of Army pictures, training films—that is big, big business, and their end of it, they had a commitment each time to finance. Of course, they [13] looked to finance in 1947. Starting in 1946 and this year 1947 that we are concerned with, they looked to finance so-called pre-production. That is before the camera turns and you have no film to show. That is the most dangerous period, the biggest gamble of all because you may never have a film. If you have a film, at least you have something tangible, but that first money, the so-called pre-production money, the money you spend before the thing starts to jell, that money demands also the highest profits. As a result, we have \$80,000.00, \$50,000.00 and \$30,000.00 going into one certain film, this Copacabana picture, and he wound up by owning fifty per cent of the picture because they took the big risk, they went through tough sledding and they were entitled to a bigger piece of it. They watched it and worked on it.

The most remarkable thing in this whole case—and I will say to you, ladies and gentlemen, Mrs. Rorke, Mr. Snider and Mrs. Saudient—suppose that the three of you and myself got together and we had a contract, and our contract said we are going to be partners, and the contract says we are going to go into the picture-financing business. That is our contract, and somebody comes along and says, “You people may have agreed to go into the picture-fi-

financing business, or you may have agreed to get into a partnership to go into the building business, but we are going to file an answer and say "No, you are not in that business." Amazing isn't it? I [14] think you would be upset and I would be, and I am. Here we have Koch & Sons, this partnership between the four children, their business having started on January 1, 1942, on October 23, 1944, amended their partnership agreement, which is Exhibit 2 in this case, and this agreement says very plainly, "The said partnership business will, in addition to engaging in those activities referred to in the existing partnership agreement, engage in the business of financing motion picture productions, either by direct participation in such productions, by way of stock investments or loans to motion picture producers, or in any other form of financing the parties may mutually agree upon between themselves."

Here these people have a solemn contract with all four of their names on it, back in 1944 drawn up, way before the year 1947, in which they say, "We partners, in addition to being in the luggage business, we are going to branch out and go in the big business of motion picture financing. This is our business."

Lo and behold, the only question raised in this case by the Government really, the only thing they deny is, we are in the motion picture financing business. That is the only thing you are called upon to pass upon in this case. Were we or were we not? I say again, if you and I had such an agreement, if Mr. Snider had such an agreement, Mr. Phipps had such

an agreement, and somebody else has denied it and [15] you have to come to court and prove your case, you could see the position we are in. Of course, when you sue the Government you can't come in and sit down in a chair and win your law suit. We have the burden of proof. The plaintiff has to prove his case by a preponderance of the evidence. I believe the Court is going to tell you in this case that preponderance of the evidence is no difficult term. It merely means by evidence that when weighed with that opposed to it has more convincing force and in which it follows there is a greater probability of truth which lies therein. It is our duty to come in here and put on a case. We can't sit down and win the law suit. They have answered it and said we are not in the business of motion picture financing. We have to come in and prove that we had activities in that business, put in exhibits to show that we were so engaged. I know you won't be misled, won't be led by anything but a rule of reason. The evidence preponderates—that means if you have 10 pounds on one side and 10 pounds and one ounce on the other side, that the 10 pounds and one ounce preponderates over the 10 pounds. It is as simple as that.

In this case the evidence is clear. With all the stress, strain, and effort that they went through this entire year of 1947, and this money these people had tied up in that business, all their hopes and aspirations tied up in it, they were engaged in the business, and I say to you they could have [16] done one-tenth—one-tenth of what they did and still be regularly engaged in the business of financing mo-



tion pictures. They could have done one-tenth less than what they proved in this courtroom and still be engaged in the business of financing motion pictures, and it would not have mattered, ladies and gentlemen, in my opinion, whether any picture was ever made, whether any story was ever bought, whether any corporation was ever formed.

In that regard, you know about corporations. You call your lawyer and order a corporation just like you call your car dealer and order a Ford. Of course, that Ford is not going to drive itself. Somebody has to drive it. A human being has to drive it. It is not going to run without gasoline in the tank and that is the money you put in the corporation.

I believe counsel for the defendant will have a statement to make at this time and I will return with our rebuttal at some later time.

Thank you. [17]

### CLOSING ARGUMENT ON BEHALF OF THE PLAINTIFF

Mr. Fink: Those of us who have devoted our lives to the law must at times bow our heads in shame when we realize that in this very country of ours, before the courts of this United States, and perhaps only over a hundred years ago, however, people who were on trial were condemned to death for witchcraft only because attorneys were able to convince the people to believe evil when a half-decayed civilization would rather believe evil than good. I know, however, that we have selected you

people on this jury. I know that Mrs. Ernst, Mrs. Moses, Mr. Hamilton, Mr. Snider and the rest of you good people are not going to believe evil instead of good. You are not going to let evil make up for the fact that the defendant in this case has not produced one scintilla of evidence. With all the United States Attorneys' offices all over the country, with all the Treasury Department men and all the F.B.I., not one single bit of evidence of any kind that we could refute here in this case has been produced, not one iota.

An argument is made here in which everybody is a crook and everybody is evil. We start out——

Mr. Gillard: I am going to take exception to that, if your Honor please. I made no allegation of anybody being a crook or anybody being evil or anything else.

The Court: Proceed, counsel. [18]

Mr. Fink: Thank you, your Honor.

Everybody who testified in this courtroom was untruthful, that myself and Professor Schiller here are trying to slip something over, and when it is all said and done, ladies and gentlemen, when I told you the story about the law suit, just awhile ago, I forgot to tell you one thing, and that is that the lawyers such as counsel here who try many cases can argue anything, both sides of anything, no matter how right or how wrong. If you haven't got the facts, if you haven't got the truth, if you haven't got the right or the fairness, then you can't try the case; you try the counsel, you try the witnesses, you try to inject a poisonous venom of mistrust.

This is kind of routine and shameful, but I know that good people in this community, this world of ours, neighbors of my clients are not going to be misled into deliberate, unnecessary mistrust of anybody.

Counsel starts out and tells you it is the second crack at this case. You know, I have no quarrel with our system of government. I think it is the greatest system in the world, and if it was not, it is the best we know of. We don't know of any better system to administer things, and yet we can't say anything is perfect, can we? We know that in this country there must be, between individuals and corporations, a hundred million tax returns, or some such quantity, and they would fill up half this town if they were stacked in one place. [19] Some fellow in San Francisco or Washington sitting there looking at that pile of tax returns, claims for refund—and, by the way, who has had a lot of them that were not fair—there is no use kidding ourselves; there are people who would like to pay less tax rather than more—at a time when you have worked on stacks of those things, you get to the point where you distrust everybody and you get a frame of mind, which is human nature, that the Government is always right and the taxpayer is always wrong.

If we had not paid this tax in the first place, I do not think there would be any question of any law suit. They wouldn't sue us for the money. We paid the tax and they say, "Let them prove their case." That is what the counsel calls our second crack. This is our clear opportunity, ladies and gen-

tlemen. This courtroom has had many cases, it will have many more. His Honor will preside over them. Counsel has other cases. Some day I may have another case. But so far as the Kochs are concerned, this is their only case, their only chance to come before a jury of their neighbors to get justice.

When you start to nail up a box, ladies and gentlemen, sometimes you can ail it down with one nail. Counsel said when I picked up the agreement which says, "We are agreed that our business is the picture business," he says Mr. Fink believed that—and I do, by the way—he said, "Why did he [20] put in any other testimony at all?" The story is, ladies and gentlemen, that even though you can nail a box down with one nail, any lawyer knows you might as well put a few more nails in it and make it good and tight.

Counsel contends that you have a non-business bad debt if it arose from the situation that is only a casual or an isolated transaction, and I think His Honor will tell you that that is the law. If a transaction is an isolated thing, separate and apart from your business and only happens rarely, an isolated transaction, it is not a deductible loss under, the theory we have taken, so that it becomes a matter of importance to look into other things, and other things are proper to be proved, other nails we can drive into this box to nail it down.

We can show we had activities, we can show it was not just isolated; we had activities, spent time and money in connection with the picture business to show we were in the business of financing motion

pictures. By the way, we did not produce any pictures and do not claim that; we say nothing about producing. We are not actors, directors or writers, we wouldn't know how to paint a set or stage. We are financing picture ventures. That is how we got hooked, stuck. .

So that in addition to the obvious evidence in this case, we have the right to drive these additional nails by proving we spent time on other deals. Whether a deal was ever [21] concluded or not, does not make one whit of difference in this case. The question is, did we spend time and effort on it? That is all. Nothing more.

I believe His Honor is going to tell you—I am not sure, but I believe the instruction will be, if you listen for it, you will hear that you may consider the amount of time spent. Spent where? In the business of financing motion pictures. When you start financing something that was not there—this is not financing U. S. Steel Corporation or Standard Oil Company. This is financing companies that were never there to begin with. You have to start somewhere. We have to prove that we were in business, that among other things, when we were getting into it, we were actively engaged in trying to finance pictures and spent our time on it. That is all. Simple.

He talked about Frank Farilla, for example, the changing of books, making erasures. The only thing that whole transaction was offered for was to show the trouble Maury Koch or the Kochs went to to borrow money even for this picture financing. That is all they came in for in the first place. If Maury

had borrowed the money from John Jones or from any one of you ladies and gentlemen and spent time borrowing it, he got it. Of course, it came in on checks signed by Frank Farilla, and the books show that later on Maury said, "Don't do that. I owe Frank the money." So they changed the book to show it was Maury's money. It is that simple. It doesn't mean anything. [22]

But it does mean this, that not only were these people trying to finance moving pictures in the year 1947—and, by the way, I have not proved with respect to other years, we all know the time in question, 1947, the transactions that had something to do with that year. The only thing that \$15,000.00 Frank Farilla deal does is to give you additional proof that not only did they use every dime they had, but they went out and begged and borrowed everything they could for this business. That is all that deal was all about. And here the cross-examination and the insidious insinuations is a little bit disturbing, ladies and gentlemen. I hope you will bear with me on that. I am not very much persuaded by this argument that we should have deducted the loss in some way.

Our loss on Copacabana was \$75,000.00. That does not mean that \$75,000.00 is in tax money. You split that \$75,000.00 between the seven people and you get \$7,500.00 per person, and then you have to take it in your tax bracket. If you are in the 20% bracket, you get 20% back. We are not trying to get \$75,000.00 from the Government, you understand that. That does not mean our taxes would be af-

fectured to that extent. Only a small fraction of that. So it is not the most tremendous amount of money involved in this suit, but there is a principle involved. Any time an American citizen in your community has five cents coming, he is entitled to it [23] and he should have it. That is justice. That is the justice that we live and die for.

Counsel spoke about me—I guess I should not include Professor Schiller in this remark—we are like a destroyer laying down a smokescreen concealing everything. If I have concealed anything from you or attempted to take advantage of any situation under the sun, please forgive me because it was not intentional, and I think I can say without apology that every person who took the witness stand in this courtroom were good people. Let us not condemn anybody because they love Maury Koch. By the way, Maury Koch, super-salesman, as counsel makes him out, is probably a good salesman because of one thing. He is a very simple, straight-forward man of very simple words. He does have a little trouble expressing himself, but he is the kind of person I trust, you trust and people trust, because he is the simple kind that tried to explain himself as best he can. He wants nothing except what is his and what belongs to his sister and brothers. They have fought side by side for a long time and they are again here. They are finally in the courtroom.

Counsel said the contract says—I don't quite follow him—but for some reason Maury Koch was doing things beyond the contract; therefore it is not partnership business. The contract says all the

assets of the partnership are available for the picture business. I think His Honor will tell you the [24] act of one partner is binding on all the partners. There is no question about that. You use a contract one way and then use it just the opposite. I don't know what he is talking about. But I believe the Court's instruction on the law will tell you one partner's acts is the acts of all the partners.

He talked about Hill of the Hawk. The partnership didn't have the money. Of course, Mr. Koch told you they didn't have the money, he put the money up, sold out a couple of years later, got the money back and that was the end of that. But no matter what he did in the partnership business, it is covered by the contract, the partnership contract of the parties. Whether he invested more money than any other person or less money than any other person, of course, he did it for all of them. I don't doubt for a minute he would not be in this business on his own behalf, but that doesn't make any difference. We are going to show the various activities. This is not a case where he wanted and bought some stock in U. S. Steel Corporation, which would be an isolated transaction. This was a business. You start something where there is nothing. You go along with it and provide the financial management. You can have all the creative people in the world but somebody has got to say to them, "You got the money. I will be responsible for this," and that is what the Kochs did. I don't see how counsel can sneeze at that million dollars from the bank. There was the \$50,000.00 for Producers' [25] Finance



Corporation, which was organized by the Kochs through their lawyer with some dummies on the Articles. I don't see how we can overlook anything when these people spent money or the expenses borne by the partnership through all these transactions over the years.

Maury Koch's time was available. I think counsel has made that point, anyhow. His time was available to the partnership and the partner gave his available time. They had the right to use it. They gave this valuable time to this business. As far as whether or not he was engaged regularly in the business, ladies and gentlemen, I am a lawyer, and if I never won a case, I am still in the business of being a lawyer.

I will tell you something else. If I open my business this morning and never had a law suit or a client, I'm still a lawyer. You don't have to win law suits for clients to be successful. The question is, "What are you spending your time at? Is it a business?" That is a plain, ordinary term. You are either doing business or you are not doing business. It is just that simple.

Counsel said the letter, Exhibit 34, is inconsistent. Maury Koch was not writing a letter to counsel or the Judge. He was not trying a law suit when he wrote this letter. He wrote to his lawyer and he said—by the way, if anybody ever had an agent in a lawyer, he knows a lawyer is always his agent, but it is not a question whether somebody is your agent or not, [26] the question in this case is, if somebody does something for you, it is just like

your own activity. In other words, if you have something done, it is like you did it yourself. If Maury Koch sends me \$25,000.00 and says, "Buy a story," it is like he bought it himself, like William Koch bought it, Beck bought it or one of the other Kochs, and when he writes me a letter, he was not preparing for any law suit. Don't believe for a minute because something stands in the name of one partner, it does not belong to all. That is ridiculous and the contrary to every bit of law under the common law since the time of William the Conqueror.

He talked about the \$8,000.00 that came from Producers' Finance Corporation which, of course, Koch put into Producers' Finance Corporation. He put \$60,000.00 into that. All these things, whether he did or whether he did not, are not important. The Kochs spent their money, they spent valuable time. They were looking for deals they could finance in picture ventures. They organized corporations. They set up deals to get things started. They tried and tried and they were successful in a few things. They at least made a picture in Beacon, though they lost their money. They made 30 or 40 training films for the Government. They bought a wonderful story and other things. Like any other experimentation or any other thing where you are dealing with ephemeral ideas, you have to capture them and get them together. There are a lot of failures, [27] but they were activities. That is all.

Did they just go down and write a check out or did they have activities? If all a man did was write a check out once in his life on investments from

surplus funds, obviously that is not a business. But if he kept some degree of activity going and made an effort to spend money and time, then he is in the business. Doesn't that appeal to your good common sense?

The Court: You have five minutes, Mr. Fink.

Mr. Fink: I don't know, counsel seems to think that these people got to the Pacific Bank here in San Francisco by some kind of osmosis or something. The bank knew nothing about the picture business. San Francisco was removed from the scene. The only reason that the bank made that loan—you know the reason—they trusted the Koch family. That is all. They wanted to hear about Jack Chertok, not about corporation names, because, frankly, in this whole business corporations don't do a thing. It is the people that you have to trust. It is the character, the credibility of those people. I will tell you something, ladies and gentlemen. Any time you find a San Francisco bank trusting somebody for a million dollars, you can trust them, too. When you have a picture going into million dollar deals, do you think that they would trust these Kochs if they were exaggeraters and purveyors of untruth? If you don't trust any of us, if I am a charlatan, Professor [28] Schiller is a charlatan, and if every witness who took the stand is a charlatan, the evidence is here in black and white. The whole situation itself is more than adequate to establish that the answer is yes to the interrogatory you are going to have. If you didn't believe any of us—let us remember one thing, that the great big,

wide arms of the law—you have had this case a long time, have not been able to bring in one single thing to refute one single thing to this case. Everybody has a right to have a lawyer, including the Tax Department, and every lawyer's duty is to come into court and argue his case for his client. Of course, we sometimes forget we are officers of the court and are supposed to make statements based upon facts and not just try to inject the evil and disbelief where the world should be good, and we hope it is. I believe it is good. I believe you people are good. But I believe when you go into that jury room and you deliberate in this case, it is not going to take you very long to put "yes" down on that question that is going to be handed to you. The Kochs were engaged in the business of financing motion pictures. It doesn't say "producing"; it says "financing." I know when you retire to the jury room you will deliberate the same just verdict that you would expect other jurors to deliberate for you if you were on trial in this type of case.

I do want to thank you for your attention and time in sitting through these four days of trial. [29]

The Court: We will take a recess at this time until 1:15 this afternoon. That is a little unusual time, and I want everybody to remember it and be back here so we can start at that time.

You are still under the admonition not to discuss the case or form or express an opinion on it until it is finally submitted to you.

(Whereupon a recess was taken until 1:15 o'clock p.m. this date.) [30]

ARGUMENT OF MR. GILLARD, ASSISTANT  
UNITED STATES ATTORNEY, TO THE  
JURY ON NOVEMBER 30, 1956

Mr. Gillard: Ladies and gentlemen of the jury, the normal course of closing a civil case of this type, as indicated to you by Mr. Fink, is for the plaintiff to open the argument and for the defendant to respond; and then for the plaintiff to close. The plaintiff gets the last word. He gets the opportunity to leave the last impression with you, and he hopes the best impression in the case, and the reason for that is because the plaintiff has the burden of proof.

When you talk about burden of proof, you have to understand that what is happening here is that an individual—let us forget about the Government for a minute because that is not important in your thinking—an individual says to you, “You owe me \$5.00,” and you say, “No, I do not owe you \$5.00.” And so you go to court. He gets on the stand and he says, “That man owes me \$5.00,” and that is all. You get on the stand and you say, “No, I don’t owe him \$5.00,” and that is all the evidence there is. How would a jury decide that case? Only by virtue of knowing that the plaintiff is making the claim and has the burden of proving that the money is owed to him can you reach a satisfactory conclusion to that question, and if you say that the evidence is perfectly even, that there is no reason to believe or disbelieve one party or the other, it is a complete stand-off. Under those circumstances the judgment

cannot be for the plaintiff. So the plaintiff has the burden of proof, and that means proving to you by the preponderance of the evidence admitted in the case that they are right in their contentions, that they are entitled to the sum of money that they are claiming from the defendant, the Government.

In this case, and the Court will so instruct you, I believe, there is a presumption that the Commissioner of Internal Revenue's determination is correct. You see, the plaintiff already had one crack at this case. He filed his claim for refund with the Commissioner of Internal Revenue and the Commissioner denied it.

Mr. Fink: Your Honor, I am going to enter an objection. We have not tried this case before. This is a law suit in itself.

The Court: This is the first time the case has been tried and counsel is correct. A claim has been filed.

Mr. Gillard: I will amend the word "case" and say "matter." In connection with this claim for this deduction, the matter has been presented previously by the plaintiff to the Commissioner of Internal Revenue, and contrary to what Mr. Fink told you, what the Commissioner of Internal Revenue said was, "No, you do not have a business bad debt. You have a non-business bad debt," and the Court will instruct you, I believe, [2\*] that what a non-business bad debt means is that the parties were entitled to take their losses in accordance with the provi-

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**\*Page numbering appearing at top of page of original Reporter's Transcript of Record.**

sions of the Internal Revenue Code providing for losses in the same manner as for short-term capital gains, and in denying the claims made by plaintiff, the Commissioner of Internal Revenue allowed each one of these plaintiffs on their tax returns for 1947 a deduction of \$1,000.00. That is the short-term capital gain provision. The Commissioner of Internal Revenue said, "You have taken your loss. It is a normal kind of loss that you would get by making your investment and losing it. You are entitled to this provision in the Internal Revenue Code which makes provision for that kind of loss. Each of you can take \$1,000.00 for 1947 off your income, and you can take \$1,000.00 off your income for each of the succeeding five years. That is the issue before you, as to whether or not that determination by the Commissioner of Internal Revenue is correct or whether the plaintiff is correct, that he is entitled to a different kind of tax treatment for the loss, which is admitted, which would allow him to offset it against his total income rather than \$1,000.00 per year as I have indicated for a total of six years.

Mr. Fink also made some reference to the solemn contracts of the parties, which is Exhibit 2 herein, and he said to you, "If some of the jurors and I had entered into this contract, and we said we were going to engage in this business, and then [3] the Government came along and said you were not in that business, you would be surprised, you would be amazed, you would be insulted."

The answer to that proposition is two-fold, ladies and gentlemen. If Mr. Fink really believed that all

there was to this case was this contract that the parties entered into, and that in and of itself and by itself was sufficient to sustain the claim, he would have put that contract into evidence and rested, period. But obviously an agreement to do something is not doing it. You heard, for example, the questions directed to the attorney, Mr. Grupp, on the stand by the Court, and he explained what happened in the incorporation. The Articles of Incorporation are also a contract. They are filed with the Secretary of State but they just sit there. There is no business being conducted at that time. You have to do something in the future in order to be in business. The fact that you say to yourself, for example, "I am going to go into the motion picture business," that does not put you in the motion picture business. The fact that you and I together say, "Let's go into the motion picture business," doesn't put us into the business. You have got to do something to be in business, and that is why Mr. Fink did not just put this contract in evidence and rest. It does not have the force and effect that he maintains it does have. It is just an indication of what they desire to do in the future. The [4] question is, What did they do in the future?

The third thing that strikes me about Mr. Fink's opening statement to you is a thing which has been peculiar throughout this entire case. It seems to me it is more like a smoke screen that a destroyer lays down to hide the real issues, in that case the target, in this case the real issues in the case. He talked to



you in grand and glowing terms about the motion picture business. He talked to you about getting the story, getting the stars, getting the director, studios, cameras, officers, staff and ideas. He talked about the resale of the picture. He said it was a business of experimentation. Ladies and gentlemen, the Kochs were not in the business of experimentation. The Kochs were not in the business of securing stories or stars, studios, cameras or officers. That is the motion picture business, and this entire case and most of the evidence that has come from the witness stand and almost all Mr. Fink's argument has been directed to deceiving you as to what the issue in this case is. The issue is not whether the Kochs are in the motion picture business; the question which will be submitted by the Court for answering is, "Were the Koch family regularly in 1947 engaged in the business of financing motion picture productions?"

Now, if the Kochs had wanted to be in the motion picture business, their partnership would have provided something like the Articles of Co-partnership of Ambassador Pictures Corporation, [5] which say, "The purpose for which this corporation is formed is generally to engage in creating, photographing, manufacturing, exhibiting, exploiting and otherwise dealing with respect to motion pictures."

Or even it would have been the same as the Articles of Partnership between Hirsch and Sebastian: "It is the purpose of the parties to hereby form and create a general partnership for the purpose of engaging in the business of producing mo-

tion picture photo supplies by use of partnership-owned means, etc.”

But that is not what the Kochs were doing, ladies and gentlemen. That is not even what they intended to do. The said partnership business will, in addition to the luggage business, engage in the business of financing motion picture productions either by direct participation in such productions, by way of stock investments or loans to motion picture producers, and therefore, pursuant to those Articles of Partnership, the question the Court is going to submit to you is, Were the Kochs in the business of financing motion pictures? Not were they in the motion picture business, a very limited phase of that whole operation. And so what you have seen in this case is an attempt to give you this big broad picture of what the motion picture business is and to show Mr. Koch moving around and talking to all these people and saying, “Well, he must be in the motion picture business.” But that is not the question. [6]

You will recall I asked Mr. Koch on the witness stand, “And all of your activities were under and pursuant to the authority contained in your partnership articles?”

And he said, “Yes.” Ladies and gentlemen, anything that Mr. Koch did that was in excess of the authority contained in these articles of partnership was unauthorized, and the Court will instruct you that only the activities of Mr. Koch which were authorized under the partnership articles can be considered to be partnership business. You cannot have an agreement to do one thing and have a man

go out and do something else and bind you. If you have agreed with another individual to sell something, and that is all, he can't bind you by going out and making a contract to buy something else. You would not be bound by that.

In this case Mr. Koch was authorized to finance motion pictures; that is all, by stock participation or direct loans. That is his only authority. Anything he did beyond that was beyond the scope of his authority and not binding upon the partnership nor of benefit to the partnership.

Mr. Fink also made a very moving statement with reference to one-for-all and all-for-one. I am going to get into that later, but preliminarily I am going to call your attention to the fact that with reference to the Ambassador Pictures Corporation, Mr. Maurice Koch invested his own money. He said if you will recall, from the stand, the partnership did not [7] have any money and he invested his own money. When the assets he had acquired in that fashion were sold, he got the money back and put it in his pocket. "All-for-one and one-for-all"—maybe so, but that is an example of the fact that everything Mr. Fink has told you is not exactly true. To find out what the evidence is which you should properly consider to determine the question the Court is going to submit to you, "Was H. Koch & Sons in the business of financing motion picture productions," you should look at these facts.

The loss that was incurred in Copacabana was admittedly financed by the partnership. It was admittedly an investment in that film and it was

admittedly lost. The reason why you have had all this other evidence and this other testimony, in addition to the Copacabana affair, is because the plaintiffs realize that that one transaction, standing by itself, is insufficient for you to find that they were regularly engaged in that business of financing motion picture productions. You can't reach into your pocket and make an investment in one instance and that is all, and come to the conclusion that you are regularly engaged in business, because, one, a discussion does not constitute a business. It is an isolated investment and that is all it is. Therefore, in order to try to buttress their case and to show that this one transaction was something other than it normally would be, they tried to produce in here other evidence to show that by virtue of other activities, [8] they were engaged in the business of financing. That other business, then, would reflect upon what they did in Copacabana and allow you to come to the conclusion that they were in the business of financing.

Let's see how successful this other evidence is. You will remember that I asked Mr. Koch—this was towards the close of the cross-examination—"Mr. Koch, What other investments were made by H. Koch & Sons during the years 1946 and 1947?"

He said, "None," and he was very crest-fallen.

I said, "What other investments were made in 1946 and 1947 which resulted in the production of motion pictures?"

The answer again was "None." Ladies and gentlemen, you have here during the critical period the

Copacabana venture and that is all you do have. All the rest of these activities that were engaged in were either attempts or they were intents or wishful thinking of some kind, but, ladies and gentlemen, we submit to you that the intention or desire of the party does not put him into the business of financing any more than the intention or desire expressed in the articles puts them into business. You have got to do something tangible. The question is, "Did he finance motion picture productions in 1947?" You are perfectly at liberty in drawing your conclusion in that, and I think properly you should disregard in reaching you final conclusion the attempts which resulted in nothing. [9]

We had an awful lot of activity, as evidenced by the testimony from the witness stand, in things which never even resulted in any kind of financial deal at all. For example, all of Mr. Koch's talk about Monogram Pictures, Al Green and his six pictures, and the Fred Fisher story—we had an awful lot of talk about those things, but we had very little financing—in fact, we had no financing at all.

I think about half your time in this courtroom has been taken up with hearing about "The Hill of the Hawk." That was apparently a very fabulous thing, and every witness on the stand has talked about "The Hill of the Hawk," and again what was the financing on that?

Incidentally, "Hill of the Hawk," as you will recall, was dropped on the recommendation of Mr. David Sebastian. It was a little difficult, you will recall, for me to get him to admit on the witness

stand that he had made the recommendation. He tried to attribute the decision to Maury Koch. The other witnesses have all tried to help Maury Koch, and that was a logical thing for them to do, because they are closely associated with him. He tried to help him out by passing that over to him, but he finally had to admit that he had made the recommendation after reading the script, that it would not make a good picture, and Maury Koch got his money back. No financing.

The interesting thing about the financing side of that [10] is that this was not partnership money at all. Everything we have heard about the "Hill of the Hawk" and all the ramifications of it were not partnership business, not one single iota of it. Let me read you from the partnership agreement, paragraph 2(a):

"Moneys advanced by individual partners over and above the sum advanced by this partnership shall be first refunded to such partner individually.

"(c) The profit on such sum or sums advanced by any one or more partners over and above that advanced by the other partners shall belong to the individual partner or partners advancing the excess."

Maury Koch said when he got his money back from this "Hill of the Hawk" venture by the sale of the stock in Ambassador Pictures and the sale of the rights that he put the money into his pocket. It didn't go into the partnership. It just so happened that the money that he got back was exactly the same amount that he put in.

I pose to you the question, What would happen if Maury Koch had made \$25,000.00 on it? Wouldn't it likewise have gone into his pocket under the partnership agreement? He was required to do so. The partnership had required and allowed him to take that profit all by himself. That is just speculative. It is not necessary for us to answer it, but it demonstrates this was Maury Koch's own affair, and I believe the [11] Court will instruct you that if you find in any one of these transactions Maury Koch was acting on his own individual behalf, that transaction cannot be taken into consideration by you in determining whether H. Koch & Sons was in the business of financing motion picture productions.

What did Maury do in this Ambassador Pictures thing? First, he took his own money, \$7,000.00, and bought all the stock in the Ambassador Pictures Corporation. After he had all the stock, he took \$10,000.00 more of his own money and loaned it to himself as sole stockholder in Ambassador Pictures. And then third—and this was rather cute—as President of Producers' Finance Corporation he loaned himself as sole stockholder of Ambassador Pictures Corporation, another \$8,000. The cute part about that was, on direct examination Mr. Koch only put into evidence, or Mr. Fink got evidence through Mr. Koch only on the letter transmitting that \$8,000.00 check. That was Exhibit 34. The letter on the letter-head of H. Koch & Sons, Luggage Manufacturing, was addressed to Mr. Max Fink:

“Dear Max: Enclosed you will find the last pay-

ment, which is \$8,000.00, for the book 'Hill of the Hawk.' Sincerely, Maury."

Mr. Fink I think you ought to read the letter, counsel.

Mr. Gillard: I will read whatever part I desire, counsel, and you may read whatever part you desire.

But he did not put the check in evidence. The check was [12] enclosed, but he did not put it in evidence. You may recall I had to ask for the check on cross-examination. Mr. Fink finally produced it, and I asked Mr. Koch, "Was this the check that was mailed with Exhibit 34?"

And he said, "Yes."

That check turned out to be a check of Producers' Finance Corporation. They did not want to let you know about that too easily, but the letter transmitting it was a letter on the Koch Manufacturing letterhead, not a letter from Producers' Finance, signed by Maury P. Koch, president.

So the total amount of money that Mr. Koch invested in this thing was \$17,000.00, not \$25,000.00 as they wanted you to believe in the first place.

Secondly, it was all Mr. Koch's personal money and not partnership money. Therefore, ladies and gentlemen, I believe under the instructions you will receive from the Court you can and should disregard all testimony with reference to Ambassador Pictures Company, with reference to the "Hill of the Hawk," with reference to any other activities Mr. Koch engaged in in that connection.

What other financing activities were there? There was only one other than that, and that was Pro-



ducers' Finance Corporation, which was formed, you will recall from Mr. Grupp's testimony, and the articles are in evidence, in about October of 1947. But the negotiations with reference to any activities [13] that that corporation was going to engage in were not concluded in 1947. As a matter of fact, very little had been done. One exhibit in this case which the defense put into evidence was a letter from Maury P. Koch, a letter from Producers' Finance Corporation by Maury P. Koch to Mr. Jack Chertok, setting forth in preliminary form their oral understanding prior to the time that anything could be reduced to formal agreement by their attorneys. At this time, in January 29, 1948, not one cent of money had been put into Producers' Finance Corporation by anybody, and that is why Mr. Koch had to say in response to my question, "No other money was spent by the partnership in 1947 and 1948, no money except the Copacabana loan was advanced during the years in issue in this suit," because, as I have just explained to you, the Ambassador Picture thing is out so far as the partnership is concerned. Mr. Koch admitted on the stand that in 1946 and 1947 the partnership advanced nothing except the Copacabana deal. The Court indicated to you that you could try and relate that back to the activities of 1947 the financing that took place in 1948 insofar as you believe those things are pertinent to the activities in 1947. However, there is one other very interesting thing about that and that is that Producers' Finance Corporation in 1948 lent some money to Apex Film Corporation for the

purpose of producing some Army training films. The witnesses have indicated some Army training films [14] were produced, but we do not know when they came out. So far as the record shows, they came out this year. We do not know. But the most interesting thing is that it was indicated by Maury Koch on the witness stand, indicated to you by Mr. Fink in his opening argument, that Maury Koch got a million dollars of financing for them in that connection. I think the Pacific National Bank would be interested in that, because my recollection is that Pacific National Bank advanced that money and the Pacific National Bank advanced it not to Maury Koch but to Apex Films Corporation. Maury Koch was not advancing in that transaction in any way. The loan was from the bank to them.

The other interesting thing about this, the most that could be said is that Maury Koch had had a hand in introducing Mr. Chertok to the bank, making a sufficient recommendation to the bank that they would be interested, and the most Mr. Koch is doing is acting as a broker. He is bringing two people together to see if they can't arrange a loan between them. Mr. Koch is not in the brokerage business. His business is advancing the money of H. Koch & Sons in motion picture productions. His business is not acting as a broker for somebody else.

Even if you would assume that that activity of his in 1946 and 1947 was a relevant and material thing as far as time was concerned, it would not be relevant as far as the business of H. Koch & Sons is concerned.

I think we ought to devote a little time to the witnesses [15] who appeared on behalf of Mr. Koch. First in order of appearance was Mr. Grupp. He had been his attorney for a number of years, an attorney who was deeply indebted to him and his family by virtue of favors given to him by Mr. Koch's father, so deeply indebted that for 20 years he worked for the Koch family and during all this period of time for H. Koch & Sons, particularly for Maurice P. Koch, for nothing—a man so deeply indebted that he worked for nothing. And if you can believe Mr. Grupp's testimony as to the amount of time he spent with Mr. Koch in these transactions, it comes almost to one-third of his time in each year, 1947 and 1948. Mr. Grupp, according to his testimony, spent one-third of all of his time in those two years for nothing. I think you can rightly say that there is an exaggeration somewhere in that testimony.

Secondly, Mr. Grupp is an attorney and he knows the difference between corporations and partnerships. He formed both of these for the Koch family. He drew up the Articles of Co-partnership and he drew up the Articles of Incorporation for Producers' Finance, and yet on the stand under direct examination he testified that all during the year 1947 he was acting for H. Koch & Sons as their attorney. But when the Producers' Finance Corporation was formed as a corporation, and he was counsel for that corporation, in all activities the corporation had he was counsel for the corporation and not for H. Koch & Sons. And you heard him admit to me

on [16] cross-examination that on the date of the incorporation he was counsel for Producers' Finance Corporation.

Then there was Mr. Sebastian. He is brother-in-law of Mr. Koch, and as such deeply interested in him. In addition to that, Mr. Sebastian had left a job which paid him a salary, I assume, with Columbia Pictures for the purpose of trying to make a living, and yet if you can believe his story, he worked hundreds of hours in conferences. He went over his time schedule also and it amounted to days, weeks and months, for nothing—for Mr. Koch for nothing. He said, "He paid me a little expense money," and he maintained during his testimony on direct examination that he was the agent for Mr. Koch—for nothing—and he maintained on cross-examination that he was the agent for Mr. Koch, again working for nothing. That is, he maintained that until I introduced in evidence the Articles of Co-partnership between himself and Mr. Hirsch, and you will recall that Mr. Sebastian became, I believe, the associate producer in Copacabana. Here is what the Articles of Co-partnership between Hirsch and Sebastian provide:

"It is contemplated by the parties hereto that the motion pictures may be produced by corporations specially organized for that purpose and which Hirsch & Sebastian, or either of them, may become an officer, director or employee. It is understood and agreed that the parties may act as such officer, director or employee of such [17] corporation, but all proceeds in the form of bonuses, salaries, or any

other thing of value which may be paid or turned over to either Hirsch or Sebastian as officer, director or employee shall be delivered forthwith to the partnership in accordance with the terms and purposes of this agreement."

Despite his conclusion that he was the agent for Mr. Koch, Mr. Sebastian was a partner of Mr. Hirsch and bound under the terms of this partnership agreement to act on behalf of Hirsch & Sebastian, and he worked for Hirsch & Sebastian, and even if he were employed individually by a corporation—and he was—that those profits, salary, would go into that partnership.

Ladies and gentlemen, he was not Mr. Koch's agent. He was an independent contractor. He has a mission to perform for himself. He had to leave. He had to get a job. One way he could get a job was to try to get Mr. Koch interested in putting some money into a deal where he could get a job as a producer or an associate producer, or whatever he was.

Mr. Eisenberg spent a long time in Hollywood. We do not know his relations with the Koch family. We presume inferentially that Hirsch & Sebastian, we have heard some indication that Hirsch & Sebastian were stockholders in Beacon Pictures Corporation. Mr. Eisenberg was hired by Beacon Pictures Corporation as a controller. There is some relationship and some close relationship between them and Mr. Koch. He was [18] hired as a controller. The controller is supposed to be there to find out that the moneys are spent properly that are avail-

able. Mr. Eisenberg in his eagerness to help Mr. Koch in this case abdicated his job as controller. Mr. Koch, he said, went over the figures on the budget, and on direct examination he said Mr. Koch made suggestions with reference to cutting down some sets, cutting out some dance routines, and if Mr. Koch had not done that, the picture would have gone over its budget.

First, wouldn't you assume that that would be the job of the controller? Secondly, on cross-examination I asked Mr. Eisenberg, Wasn't the budget less than the available moneys? And he said, "Yes." The budget was already below the available moneys, and yet he got up here in his enthusiasm, and again I do not blame him because you know and I know that Mr. Maury Koch is a personable and charming man, but he did a lot of selling on this witness stand. He is a salesman. He has done a lot of favors for these witnesses and they, to the best of their ability, are going to return it. I do not mean to infer that these men are deliberately misstating, but in their enthusiasm they went too far. The fact remains that the budget was less than the available moneys, and therefore it would have been impossible for Mr. Eisenberg to say that if Maury Koch had not cut these items out of the budget, the picture would have cost more than the amount of money available. So in his [19] enthusiasm of helping Mr. Koch, he went a little too far.

I say each of those three witnesses were very partisan witnesses, and you have a perfect right to view with skepticism some of their exaggerations.

Mrs. Abel, the testimony she gave concerns a matter which is not going to be presented to you for decision, and so it is not important to discuss her except one thing is apparent. Here again you have a witness who is willing to go overboard for Mr. Maury Koch. At his direction she altered the partnership books—altered them, and came in here with a set of books and tried to reflect something that did not originally occur on those books.

The Court: Is this a convenient place to take a recess, counsel?

Mr. Gillard: Yes, your Honor.

(Recess.)

Mr. Gillard: Thank you, your Honor. The watch is for timing. Each side has been allotted a definite period of time in which to present what it hopes to be its enlightenment of the case, and according to my calculations I have about 20 minutes left.

The key and central figure in this case, of course, is Maurice P. Koch, and he obviously is a very likeable man. He is obviously a very jolly man. He is a salesman in the best sense of the word. His business is selling and, of [20] course, one of the things he was doing on the stand is one of the things he has devoted his life to, and that is selling, and his purpose in being here today was to sell his side of the story to you. The thing about it, however, is that he has lived with this experience for the past ten years, and as so often happens in our experiences, the further we get away perhaps from a given event, the more dim becomes the individual

details, and the broader becomes the outline and the broad aspects of it, and we tend to exaggerate not only the importance of events, but our participation in those events. To a man like Maury, affable, extrovert type, he would naturally place more emphasis on the pronoun "I" than was warranted by the original facts. It also make a better story. You know perfectly well a fisherman does not like to come home and say he caught a fish that was that long (indicating). It makes a better story to say the fish was that big (indicating). I think we have quite a bit of that presented to you in this case by Maury Koch.

You may recall, for example, on direct examination he went down and spent three weeks in Hollywood at the time Copacabana was about to be filmed. He went in there and he went over the budget, cut costs, he cut out sets, he cut out dance routines, he fired a couple of writers, he viewed the film, and after each day he made suggestions as to the cutting of the film. It is kind of odd almost to hear him say on [21] cross-examination that the film had a producer, a director, an associate producer, controller, property man, filming editors, and all the rest of those employees. But apparently, as I say, the story has been enlarged in Mr. Koch's mind—and I do not say this in any derogatory sense; it is a normal human tendency to enlarge our own activities, and I believe you can rightly find that there has been a great deal of exaggeration in this case. This exaggeration with reference to non-important details—and I say that because actually, although



Mr. Koch had a legitimate right to be in Hollywood—I mean, he was a substantial investor in Copacabana and as such he was interested in seeing what they were doing down there with part of his money—still, properly speaking, would you say that that was a necessary function or a proper function for him to engage in under the partnership articles which allowed him to invest or to lend money for motion picture production? He certainly was interested. He wanted to see what was going to happen to his money. But for him even to suggest that he is engaged in these other activities—even assuming he did—does not necessarily make it a legitimate function. You will recall the testimony of Mr. Eisenberg that the budget was less than the available moneys.

But for some of the more important evidence this tendency to exaggerate becomes critical. For example, Mr. Koch characterized almost everybody he came in contact with as his [22] agent. Everybody he talked to throughout this entire trial, from his testimony, he would conclude was his agent. Mr. Hirsch, Mr. Sebastian, Mr. Chertok, Mr. Green, Mr. Harry Fox, maybe even Mr. Max Fink. But, ladies and gentlemen, you do not create an agency merely by having Mr. Koch say, “He was my agent.” An agency springs from a factual relationship, and in order to come to a conclusion that a given individual was an agent, there should be facts from which you can make up your own mind as to whether that agency existed. For example, under Mr. Koch’s interpretation, if any one of you were

to go out and try to buy a piece of property, you would contact the broker, you would contact the seller, you would contact the title insurance company, you would contact the bank. All those people had individual roles to play in a given transaction. Each one is hired by either himself or some other person. They are drawn together for the purpose of making that transaction. But that does not mean that the seller of the property is your agent when you are buying. It does not mean the bank is your agent in that connection for that purpose. These are all independent people who have a job to perform, who were paid by others, not paid by you, and they are only drawn together as a principal in a transaction in which they are interested, and they are not working for you.

That came about, I believe, very clearly in Mr. Koch's characterization of Mr. Sebastian as his agent. I think I [23] have shown you very clearly that Mr. Sebastian was not Mr. Koch's agent. He was a partner of Mr. Hirsch, and all his activity was devoted to the Hirsch-Sebastian partnership and for the benefit of that partnership. Mr. Sebastian was not paid one cent by Mr. Koch.

How does Mr. Sebastian become an agent? Only because Mr. Koch said so, but you do not have to rely on Mr. Koch's legal conclusion that any individual was his agent. You should examine the facts for yourself and determine whether or not Mr. Koch has presented evidence of such a relationship—a form of employment, instructions to him, payment

to him, to indicate that every man he is talking about is or is not his agent.

Another classical example of Mr. Koch's characterization of others as being agents or connected with him in some fashion is in this same Exhibit 34 that I read to you awhile ago, or a part of it. Mr. Fink tells me to read the whole thing. In that letter—and Mr. Fink read the whole thing to you—he said, “Will you please send me some sort of letter advising me that the book is completely paid for and the property of Ambassador Pictures Corporation, of which I own all of the stock now, and, after all, I am responsible to the stockholders.”

Mr. Fink asked him what he meant by that and he said, “my partners.”

Of course, the letter on its face is inconsistent for he owns all of the stock. There are no stockholders. There is [24] one stockholder and that is Mr. Koch. But in the second place it shows the thinking of Mr. Koch in this thing.

Now, you may not want to blame him, or you may feel that even he did believe it. It is very possible that he did believe it, but he was in error, ladies and gentlemen. He was in error. His partners were not stockholders in Ambassador Pictures Corporation. He owned all the stock himself, with his own money, not the partnership money, and all the money that had gone into Ambassador Pictures Corporation was his own money, and he admitted that, so that his characterization of his brothers and sisters as stockholders was erroneous. You do not have to accept his characterization of that any more

than you have to accept his characterization of all the rest of these people as being agents, unless you are satisfied from the evidence that he has demonstrated to you by facts an employment agreement, a delegation of authority, payment to him for the services. The facts alleged make it an agency relationship. If that is absent from the case, these people were not his agents.

We can only point to a few examples like that where we have demonstrated that the conclusions Mr. Koch reaches on the stand were erroneous, but from the demonstrated fact that he was in error you can ask yourselves the question, "What about all the rest of these facts he has told you about concerning which there was no possibility to rebut because the [25] witness was not available?"

Mr. Chertok is in New York, somebody else is dead. You can weigh his testimony as a whole, ladies and gentlemen of the jury, and if you find him wanting in any material respect in his testimony, you are entitled to disbelieve the rest of his testimony.

He also spent a great deal of time in generalization. As a matter of fact, Mr. Fink in his opening statement to you spent a great deal of time in generalization. The whole theory of the plaintiff's case here is to try to snow you under with motion picture business and weigh you down with so many facts and so much evidence that you can't see the issue in the case. You recall Mr. Koch testifying in response to a question by Mr. Kink, "I spent an awful lot of time trying to make deals, tie deals to-

gether, telephone conversations, making contacts with this fellow, talking to Hirsch, talking to Sebastian." What do you think of that kind of testimony? Feathers. What can you grab into with that kind of testimony which will convince you of any real thing about this case? That kind of testimony is meaningless.

You will remember during the course of this time I objected upon numerous occasions. It was never followed up. The preliminary matter was gone into:

"Did you have a discussion with Mr. Hirsch?" Yes, he did. He met Mr. Hirsch on eight separate occasions. [26]

"How about Mr. Sebastian?" The same thing. He met him at the Friars' Club, he met him here, he met him there. And what happened? Nothing. He just told you he had discussions and that is all. Is that the kind of evidence you are going to accept in this case to satisfy you that he was in the business of financing motion pictures? Mr. Koch is a very energetic man. The evidence clearly shows that he is not only energetic but in some fields he is very capable. He was the boss, the managing partner of H. Koch & Sons. During the year 1946 he was also the only salesman in that organization. That was a business grossing in sales in excess of a half million dollars a year, and he ran the show, ladies and gentlemen. He ran the whole show. He not only did all the buying, getting all the merchandise, arranging for all the financing, securing all the materials, running the place, but he did all the selling, too. \$550,000.00 worth of sales.

In addition to that he was a fifty per cent partner with Mr. Farelli in a merchandising venture in which he devoted a considerable part of his time in 1946, and from which he made a substantial profit, as you noted from his income tax return. In addition to that, at the end of 1946 he was engaged in purchasing a glass fiber plant, which I gather from the testimony is the foundation and basis for the present Koch business, the manufacture of fiberglass luggage and containers. So he was busily engaged in tangible things which you have in [27] front of you and which you can see.

Stacked against those tangible evidences of the things which occupied his time, he says he spent 30 per cent of his time in the motion picture business. Ladies and gentlemen, I think you will find that also is an exaggeration, and I think you are entitled to believe it was an exaggeration.

Now, if you disregard all the generalities in the case, which are feathers, and which you cannot put your finger on, if you find that these agents were non-existent, that each one of these people he is talking about had his own business to conduct, that he was drawn into it, came in contact with Mr. Koch because they had something to sell, something to get out of him; they were acting on behalf of themselves or their client and he was acting for himself. This was his business. If you do not attribute all their activities—and this has been the main thrust of the plaintiff's case, ladies and gentlemen of the jury—Mr. Koch has tried to graft onto himself and to take credit for everything that every-

body else did in the motion picture industry. I do not think you are going to swallow that story. Those people are down there to make a living for themselves. They may be a happy family, everybody in Hollywood, or they may not. But you can rest assured they are down there to make a living. They had to work for themselves. Mr. Koch did not pay them anything. So if you disregard all the woof about these agents, and if you [28] disregard all of these attempts which never materialized into fruition—and that is all they were—they meant no more as far as the main issue in this case is concerned than the intent expressed in the partnership agreement, “I will enter the motion picture financing business,” and he didn’t do it—if those things are left out, you wind up with the case exactly where you started, with the very first thing, Copacabana. There is nothing else in the case but Copacabana. I have demonstrated to you, I believe, that that is the only thing into which there was any money put in 1946 and 1947. It was the only picture that was produced during that period of time. It was the only transaction in which the Koch partnership put any money in that period of time. The Ambassador Picture Corporation is out completely because it is his own individual baby and not the partnership’s, and also the transactions in connection with that, including “Hill of the Hawk”—and, as I said to you, about half of your time has been spent listening to that “Hill of the Hawk” transaction, and it does not contribute one iota to this case as far as your consideration is concerned. That was Maurice

P. Koch's private baby. The partnership had no part of it.

The last thing and only thing left was Producers, in which nothing was done in 1947, no money was put into it in 1947, and in addition to that, even if you attribute to Maurice P. Koch and through him the partnership some activity [29] in 1947 for Producers, you have to remember this, that it was a corporation. You are entitled to believe and to find that when a man elects to form a corporation and do business through a corporate form, then those things that are done by that corporation are the business of the corporation. H. Koch & Sons, the partnership, was to be in the business of financing motion pictures. Ladies and gentlemen, that means H. Koch & Sons. It does not mean Producers Finance Corporation, and the very little bit of activity in this case which took place and that started at the end of 1947, and this tiny amount of it was the activity of Producers' Finance Corporation. I asked Mr. Koch on the witness stand and he told me, "Yes, everything I did from the date of the formation of that corporation, I did as the president of Producers' Finance Corporation, not as a partner of H. Koch & Sons," ladies and gentlemen, not as a partner of H. Koch and Sons. He did it as president of Producers' Finance Corporation. He gave you the answer on the witness stand: "I acted as president of Producers' Finance Corporation." That is not H. Koch & Sons.

We submit to you, ladies and gentlemen, the finding of the Commissioner of Internal Revenue.



who was a duly and regularly appointed executive officer of the Government, sworn to administer Internal Revenue Laws, that his findings that this was a non-business bad debt, and under the Internal Revenue Code provisions that each of the seven parties to this action [30] were entitled to take a deduction of \$1,000.00 per year against ordinary income for each of six years, was the correct conclusion in the case, and we submit to you that based upon the only fact remaining in the case, to wit, the Copacabana investment, we submit to you that by virtue of that one investment that you cannot find that H. Koch & Sons were in the business of regularly financing motion picture productions.

I thank you very much for your time and attention.

[Endorsed]: Filed July 18, 1957. [31]

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[Title of District Court and Cause.]

CERTIFICATE OF CLERK  
TO RECORD ON APPEAL

I, C. W. Calbreath, Clerk of the United States District Court for the Northern District of California, hereby certify the foregoing and accompanying documents and exhibits, listed below, are the originals filed in this Court in the above-entitled case and constitute the record on appeal herein as designated by the attorneys for the appellant, Except the Reporter's transcript of evidence and proceedings is not included for the reason it has not been delivered to this office for filing:

Excerpt From Docket Entries.

Complaint.

Answer.

Special Verdict.

Order Denying Motion for Judgment Notwithstanding Verdict and to Set Aside Special Verdict.

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Findings of Fact and Conclusions of Law Tendered by Defendant.

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Order Extending Time to Docket Record on Appeal.

Appellants' Designation of Record on Appeal.

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Defendant's Exhibits A, B, C, D, E, F, G, H, I, J and K.

In Witness Whereof I have hereunto set my hand and affixed the seal of said District Court this 17th day of July, 1957.

[Seal] C. W. CALBREATH,  
Clerk;

By /s/ MARGARET P. BLAIR,  
Deputy Clerk.

---

[Title of District Court and Cause.]

CERTIFICATE OF CLERK TO  
SUPPLEMENTAL RECORD ON APPEAL

I, C. W. Calbreath, Clerk of the United States District Court for the Northern District of California, hereby certify the foregoing and accompanying documents, listed below, are the originals filed in this Court in the above-entitled case and constitute the supplemental record on appeal herein as designated by the attorney for the appellant:

Reporters' Transcript of Trial, November 26, 29 and 30, 1956.

In Witness Whereof, I have hereunto set my hand and affixed the seal of said District Court this 22nd day of July, 1957.

[Seal] C. W. CALBREATH,  
Clerk;

By /s/ MARGARET P. BLAIR,  
Deputy Clerk.

[Endorsed]: No. 15645. United States Court of Appeals for the Ninth Circuit. Harold M. Koch, Bessie Koch, William L. Koch, Rose Koch, Rebecca Koch Abel, Maurice P. Koch, and Daisy Koch, Appellants, vs. United States of America, Appellee. Transcript of Record. Appeal from the United States District Court for the Northern District of California, Southern Division.

Filed July 17, 1957.

Docketed July 27, 1957.

/s/ PAUL P. O'BRIEN,  
Clerk of the United States Court of Appeals for the  
Ninth Circuit.

In the United States Court of Appeals  
for the Ninth Circuit

Civil No. 34762

HAROLD M. KOCH, et al.,

Appellants,

vs.

UNITED STATES OF AMERICA,

Appellee.

STIPULATION AND ORDER

It Is Hereby Stipulated that the exhibits designated on appeal in this action may be considered in their original form without printing, and without prejudice to either party to print any exhibits as an appendix to the brief to be filed.

Dated: August 6, 1957.

/s/ LEON SCHILLER,

Attorney for Appellants.

LLOYD H. BURKE,

United States Attorney;

By /s/ MARVIN D. MORGENSTEIN,

Assistant United States Attorney, Attorneys for  
Appellee.

/s/ ALBERT LEE STEPHENS,

/s/ RICHARD H. CHAMBERS,

/s/ FREDERICK G. HAMLEY,

Judges of the United States Court of Appeals for  
the Ninth Circuit.

[Title of Court of Appeals and Cause.]

AFFIDAVIT OF LEON SCHILLER IN SUPPORT OF STIPULATION AND ORDER RELATING TO PRINTING OF EXHIBITS

State of California,

City and County of San Francisco—ss.

Leon Schiller, being first duly sworn, deposes and says:

I am one of the attorneys for appellants in the above-entitled action. In the trial of said action, appellants offered in evidence thirty-seven exhibits, and appellee offered in evidence eleven exhibits. Many of the exhibits are quite lengthy. At this time it is not feasible for appellants to extract from these various exhibits the portions of each exhibit to which reference must be made in the briefs to be presented in this appeal. To print all the exhibits in their entirety would entail a tremendous printing cost to appellants. At the time briefs are filed with the court, counsel can distill and extract from the exhibits the portions of particular importance to the court and print them in the appendix to the brief. The granting of the order by the court will result in a substantial saving in cost to appellants and will protect the rights of both appellants and appellee.

/s/ LEON SCHILLER.

Subscribed and sworn to before me this 7th day  
of August, 1957.

[Seal]     /s/ NITA LAND,  
Notary Public in and for the City and County of  
San Francisco, State of California.

[Endorsed]: Filed August 13, 1957.

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[Title of Court of Appeals and Cause.]

STATEMENT OF POINTS UPON  
WHICH APPELLANTS RELY

The points upon which appellants intend to rely  
on this appeal are as follows:

1. That the Court erred in granting judgment  
for defendant.
2. That the verdict of the jury on the special  
interrogatory was contrary to all the evidence in  
the above cause and is not supported by the evi-  
dence.
3. That the Court erred in failing to grant a  
directed verdict in favor of plaintiffs.
4. That the Court erred in failing to grant mo-  
tion for judgment notwithstanding the verdict.
5. That the Court erred in excluding evidence,  
both oral and documentary.
6. That the Court erred in admitting evidence,  
both oral and documentary.

7. That the Court erred in failing to give necessary instructions to the jury and in giving the jury instructions contrary to law.

8. That plaintiffs were not accorded a fair trial and due process of law.

9. That plaintiffs' cause was prejudiced by reason of prejudicial misconduct of counsel for defendant.

10. That the Court erred in permitting comment upon, as well as making comment with respect to, matters not within the record in the instant cause and which prejudicially affected the trial and decision in this cause.

11. That the Court erred in granting motion for directed verdict with respect to the plaintiffs Maurice B. Koch and Daisy Koch; and likewise thereby prejudiced the rights of all other plaintiffs.

12. That the Court erred in making findings of fact which are not supported by the evidence and which are in fact contrary to all the evidence in the above cause.

13. That the Court erred in its findings and determination that certain stipulations were entered into which were, in fact, not entered into.

14. That the Court made erroneous conclusions of law.

15. That the Court erred in its judgment rendered in the above cause.



16. That the Court erred in failing to grant a mistrial in the above cause and erred in its failure to grant a new trial.

Dated: August 2, 1957.

MAX FINK,  
LEON SCHILLER,

By /s/ LEON SCHILLER,  
Counsel for Appellants.

Service of copy acknowledged.

[Endorsed]: Filed August 7, 1957.

General Assembly of the Synod of the Presbyterian Church in the United States of America, held at the City of New York, from the 1st to the 10th of May, 1776.

By James O. Easton, Secretary.

Printed by J. M. Smith,

at the Office of the Secretary, No. 10, Nassau Street.

And Sold by J. M. Smith, at the Office of the Secretary, No. 10, Nassau Street.

1776.

Printed by J. M. Smith,

at the Office of the Secretary, No. 10, Nassau Street.

By James O. Easton, Secretary.

Printed by J. M. Smith, at the Office of the Secretary, No. 10, Nassau Street.

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at the Office of the Secretary, No. 10, Nassau Street.

No. 15645

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**United States  
Court of Appeals**  
for the Ninth Circuit

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**HAROLD M. KOCH, BESSIE KOCH, WIL-  
LIAM L. KOCH, ROSE KOCH, REBECCA  
KOCH ABEL, MAURICE P. KOCH, and  
DAISY KOCH,**

Appellants,

vs.

**UNITED STATES OF AMERICA,**

Appellee.

---

**Supplemental  
Transcript of Record**

---

**Appeal from the United States District Court for the  
Northern District of California.  
Southern Division.**

**FILED**  
JAN 7 1936

PAUL P. GIBBEN, CLERK



No. 15645

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**United States**  
**Court of Appeals**  
for the Ninth Circuit

---

HAROLD M. KOCH, BESSIE KOCH, WIL-  
LIAM L. KOCH, ROSE KOCH, REBECCA  
KOCH ABEL, MAURICE P. KOCH, and  
DAISY KOCH,

Appellants,

vs.

UNITED STATES OF AMERICA,

Appellee.

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**Supplemental**  
**Transcript of Record**

---

**Appeal from the United States District Court for the**  
**Northern District of California.**  
**Southern Division.**



## INDEX

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

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In the United States District Court in and for the  
Northern District of California, Southern Division

Civil Action No. 34762

HAROLD M. KOCH, BESSIE KOCH, WIL-  
LIAM L. KOCH, ROSE KOCH, REBECCA  
KOCH ABEL, MAURICE P. KOCH and  
DAISY KOCH,

Plaintiffs,

vs.

UNITED STATES OF AMERICA,

Defendant.

COMPLAINT FOR RECOVERY OF FEDERAL  
INCOME TAXES ERRONEOUSLY AND  
ILLEGALLY COLLECTED

Comes Now Plaintiff, Harold M. Koch, and for a  
First Cause of Action Against the Defendant  
Alleges That:

I.

This action is brought against the United States  
for recovery of federal income taxes erroneously,  
illegally and wrongfully assessed and collected un-  
der the internal revenue laws of the United States;  
it is brought pursuant to the provisions of U.S.C.  
Title 28, Section 1346(a) (1).

II.

This action is to recover income taxes paid for  
the calendar years 1945 and 1947. The plaintiff's in-  
come tax returns for said years were duly filed with

## XI.

On or about January 7, 1949, plaintiff duly filed with the United States Collector of Internal Revenue for the First District of California, an original claim for refund in the amount of \$223.00, and on March 15, 1951 plaintiff filed an amended claim for refund for said \$223.00 in connection with his 1947 income tax return which represented all of the income tax paid by plaintiff on the said return; said claims were based on the grounds that plaintiff was entitled to an additional deduction on his 1947 income tax return in the amount of \$9,375.00 which was plaintiff's one half community share of his \$18,750.00 chargeable loss on the aforementioned \$75,000.00 loss. A copy of said original claim, marked Exhibit A, and a copy of said amended claim, marked Exhibit B, is attached hereto, and is incorporated by reference.

## XII.

The Commissioner of Internal Revenue, through the office of the Regional Commissioner of Internal Revenue, notified plaintiff on September 10, 1954 that said \$9,375.00 chargeable loss was a 1947 loss but that in his opinion said loss was a non-business bad debt and was therefore a capital loss and thus was deductible by petitioner in 1947 only in the amount of \$1,000.00.

## XIII.

Subsequently the amount of \$107.00 was refunded to plaintiff on the basis said loss was a capital loss

and the balance of said claims in the amount of \$116.00 was disallowed.

#### XIV.

Said disallowance of \$116.00 was wrongful, erroneous, and illegal in that said loss of \$9,375.00 was either a business bad debt, a loss incurred in the business of producing motion pictures, or a joint venture loss in the business of producing a motion picture, to wit, Copacabana, and therefore deductible in full by plaintiff.

#### XV.

No part of said sum of \$116.00 erroneously retained by defendant has been repaid or refunded, and said sum together with interest thereon as provided by law is due, unpaid and owing to plaintiff from defendant.

### Second Count

#### I.

Plaintiff, Harold M. Koch, Incorporates in This Second Count, All the Allegations Contained in Paragraphs I to X Inclusively of the First Count With the Same Force and Effect as Though Fully Set Forth Herein.

#### II.

In connection with his 1945 income tax return, plaintiff duly paid the income tax shown to be due by said return, to wit, the sum of \$8,842.22.

## III.

On or about January 7, 1949, plaintiff duly filed with the United States Collector of Internal Revenue for the First District of California, an original claim for refund in the amount of \$318.00, and on March 15, 1951, plaintiff filed an amended claim for refund for said \$318.00 in connection with her 1947 income tax return which represented all of the income tax paid by plaintiff on the said return; said claims were based on the grounds that plaintiff was entitled to an additional deduction on her 1947 income tax return in the amount of \$9,375.00, which was plaintiff's one half community share of her husband's \$18,750.00 chargeable loss on the aforementioned \$75,000.00 loss. A copy of said original claim, marked Exhibit E, and a copy of said amended claim, marked Exhibit F, is attached hereto, and is incorporated by reference.

## IV.

The Commissioner of Internal Revenue, through the Office of the Regional Commissioner of Internal Revenue, notified plaintiff on September 10, 1954, that said \$9,375.00 chargeable loss was a 1947 loss but that in his opinion said loss was a non-business bad debt and was therefore a capital loss and thus was deductible by petitioner only in the amount of \$1,000.00.

## V.

Subsequently the amount of \$107.00 was refunded to plaintiff on the basis said loss was a capital loss

and the balance of said claim in the amount of \$211.00 was disallowed.

## VI.

Said disallowance of \$211.00 was wrongful, erroneous, and illegal in that said loss of \$9,375.00 was either a business bad debt, a loss incurred in the business of producing motion pictures, or a joint venture loss in the business of producing a motion picture, to wit, Copacabana, and therefore deductible in full by plaintiff.

## VII.

No part of said sum of \$211.00 erroneously retained by defendant has been repaid or refunded, and said sum together with interest thereon as provided by law is due, unpaid, and owing to plaintiff from defendant.

## Fourth Count

### I.

Plaintiff, Bessie Koch, Incorporates in This Fourth Count, All the Allegations Contained in Paragraphs I to IX Inclusively of the First Count With the Same Force and Effect as Though Fully Set Forth Herein.

### II.

In connection with her 1945 income tax return, plaintiff duly paid the income tax shown to be due by said return, to wit, the sum of \$9,126.41.

## II.

Plaintiff and his wife, Rose Koch, filed separate returns for the year 1947, and did not claim any portion of said \$18,750.00 loss on said returns.

## III.

On or about January 7, 1949, plaintiff duly filed with the United States Collector of Internal Revenue for the First District of California, an original claim for refund in the amount of \$223.00, and on March 15, 1951 plaintiff filed an amended claim for refund for said \$223.00 in connection with his 1947 income tax return which represented all of the income tax paid by plaintiff on the said return; said claims were based on the grounds that plaintiff was entitled to an additional deduction on his 1947 income tax return in the amount of \$9,375.00, which was plaintiff's one half community share of his \$18,750.00 chargeable loss on the aforementioned \$75,000.00 loss. A copy of said original claim, marked Exhibit I, and a copy of said amended claim, marked Exhibit J, is attached hereto, and is incorporated by reference.

## IV.

The Commissioner of Internal Revenue, through the office of the Regional Commissioner of Internal Revenue, notified plaintiff on September 10, 1954 that said \$9,375.00 chargeable loss was a 1947 loss but that in his opinion said loss was a non-business bad debt and was therefore a capital loss and thus was deductible by petitioner in 1947 only in the amount of \$1,000.00.

## V.

Subsequently the amount of \$107.00 was refunded to plaintiff on the basis said loss was a capital loss and the balance of said claims in the amount of \$116.00 was disallowed.

## VI.

Said disallowance of \$116.00 was wrongful, erroneous, and illegal in that said loss of \$9,375.00 was either a business bad debt, a loss incurred in the business of producing motion pictures, or a joint venture loss in the business of producing a motion picture, to wit, Copacabana, and therefore deductible in full by plaintiff.

## VII.

No part of said sum of \$116.00 erroneously retained by defendant has been repaid or refunded, and said sum together with interest thereon as provided by law is due, unpaid and owing to plaintiff from defendant.

## Sixth Count

## I.

Plaintiff, William L. Koch, incorporates in this sixth count, all the allegations contained in Paragraphs I to IX inclusively of the first count with the same force and effect as though fully set forth herein.

## II.

In connection with his 1945 income tax return plaintiff duly paid the income tax shown to be due by said return, to wit, the sum of \$8,842.22.

## III.

Plaintiff incurred a net operating loss for the calendar year 1947 in the amount of \$6,592.72 which loss is allowable as a net operating loss deduction carryback for the calendar year 1945.

## IV.

On or about January 7, 1949, plaintiff duly filed with the United States Collector of Internal Revenue for the First District of California, an original claim for refund in the amount of \$3,623.90 in connection with said 1945 income tax return, and on March 15, 1951, plaintiff filed an amended claim for refund in the same amount of \$3,623.90. Said claims were based on the ground that plaintiff was entitled to a net operating loss deduction of \$6,592.72 for said year and in particular that plaintiff's \$18,750.00 chargeable share of the aforementioned \$75,000.00 loss was a loss from the operation of a business regularly carried on by said H. Koch & Sons. A copy of said original claim, marked Exhibit K, and a copy of said amended claim, marked Exhibit L, is attached hereto, and is incorporated by reference.

## V.

The Commissioner of Internal Revenue, through the Office of the Regional Commissioner of Internal Revenue, notified plaintiff on September 10, 1954 that his ruling was that said \$75,000.00 loss was a non-business loss and that therefore plaintiff could not include his share of said loss in a net operating loss. Said claims for refund were therefore denied.



## VI.

Said disallowance of said claims for refund was wrongful, erroneous, and illegal in that said \$75,000.00 loss and plaintiff's share of same was either a business bad debt, a loss incurred in the business of producing motion pictures, or a joint venture loss in the business of producing a motion picture, to wit, Copacabana, and in any case constituted a loss from a business regularly carried on by H. Koch & Sons and therefore by plaintiff.

## VII.

No part of said \$3,623.90 erroneously retained by defendant has been repaid or refunded, and said sum together with interest thereon as provided by law is due, payable and owing to plaintiff from Defendant.

## Seventh Count

Comes Now Plaintiff, Rose Koch, and for a Seventh Cause of Action Against the Defendant Alleges That:

## I.

Plaintiff, Rose Koch, incorporates in this seventh count, all the allegations contained in Paragraphs I to IX inclusively of the first count with the same force and effect as though fully set forth herein.

## II.

Plaintiff and her husband, William L. Koch, filed separate returns for the year 1945, and did not claim any portion of said \$18,750.00 loss on said returns.

## III.

On or about January 7, 1949, plaintiff duly filed with the United States Collector of Internal Revenue for the First District of California, an original claim for refund in the amount of \$318.00, and on March 15, 1951, plaintiff filed an amended claim for refund for said \$318.00 in connection with her 1947 income tax return which represented all of the income tax paid by plaintiff on the said return; said claims were based on the grounds that plaintiff was entitled to an additional deduction on her 1947 income tax return in the amount of \$9,375.00, which was plaintiff's one half community share of her husband's \$18,750.00 chargeable loss on the aforementioned \$75,000.00 loss. A copy of said original claim, marked Exhibit M, and a copy of said amended claim, marked Exhibit N, is attached hereto and is incorporated by reference.

## IV.

The Commissioner of Internal Revenue, through the Office of the Regional Commissioner of Internal Revenue, notified plaintiff on September 10, 1954, that said \$9,375.00 chargeable loss was a 1947 loss but that in his opinion said loss was a non-business bad debt and was therefore a capital loss and thus was deductible by petitioner only in the amount of \$1,000.00.

## V.

Subsequently the amount of \$107.00 was refunded to plaintiff on the basis said loss was a capital loss

and the balance of said claim in the amount of \$211.00 was disallowed.

#### VI.

Said disallowance of \$211.00 was wrongful, erroneous, and illegal in that said loss of \$9,375.00 was either a business bad debt, a loss incurred in the business of producing a motion picture, to wit, Copacabana, and therefore deductible in full by plaintiff.

#### VII.

No part of said sum of \$211.00 erroneously retained by defendant has been repaid or refunded, and said sum together with interest thereon as provided by law is due, unpaid, and owing to plaintiff from defendant.

### Eighth Count

#### I.

Plaintiff, Rose Koch, Incorporates in This Eighth Count, All the Allegations Contained in Paragraphs I to IX Inclusively of the First Count With the Same Force and Effect as Though Fully Set Forth Herein.

#### II.

In connection with her 1945 income tax return, plaintiff duly paid the income tax shown to be due by said return, to wit, the sum of \$9,126.41.

#### III.

Plaintiff incurred a net operating loss for the calendar year 1947 in the amount of \$6,592.72 which

loss is allowable as a net operating loss deduction carryback for the calendar year 1945.

#### IV.

On or about January 7, 1949, plaintiff duly filed with the United States Collector of Internal Revenue for the First District of California, an original claim for refund in the amount of \$3,673.08 in connection with said 1945 income tax return, and on March 15, 1951, plaintiff filed an amended claim for refund in the same amount of \$3,673.08. Said claims were based on the ground that plaintiff was entitled to a net operating loss deduction in the amount of \$6,592.72 for said year and in particular that plaintiff's community property share of her husband's \$18,750.00 chargeable share of the aforementioned \$75,000.00 loss was a loss from the operation of a business regularly carried on by said H. Koch & Sons. A copy of said original claim, marked Exhibit O, and a copy of said amended claim, marked Exhibit P, is attached hereto, and is incorporated by reference.

#### V.

The Commissioner of Internal Revenue, through the Office of the Regional Commissioner of Internal Revenue, notified plaintiff on September 10, 1954 that his ruling was that said \$75,000.00 loss was a non-business loss and that therefore plaintiff could not include her community property half of her husband's share of said partnership loss in a net operating loss. Said claims for refund were therefore denied.

## VI.

Said disallowance of said claims for refund was wrongful, erroneous, and illegal in that said \$75,000.00 loss and plaintiff's community property half of her husband's share of said partnership loss was either a business bad debt, a loss incurred in the business of producing motion pictures, or a joint venture loss in the business of producing a motion picture, to wit, Copacabana.

## VII.

No part of said sum of \$3,673.08 erroneously retained by defendant has been repaid or refunded, and said sum together with interest thereon as provided by law is due, payable and owing to plaintiff from defendant.

## Ninth Count

Comes Now Plaintiff, Rebecca Koch Abel, and for a Ninth Cause of Action Against the Defendant Alleges That:

## I.

Plaintiff, Rebecca Koch Abel, incorporates in this ninth count, all the allegations contained in Paragraphs I to IX inclusively of the first count with the same force and effect as though fully set forth herein.

## II.

On or about January 7, 1949, plaintiff duly filed with the United States Collector of Internal Revenue for the First District of California, an original

claim for refund in the amount of \$605.61, and on March 15, 1951, plaintiff filed an amended claim for refund for said \$605.61 in connection with her 1947 income tax return which represented all of the income tax paid by plaintiff on the said return; said claims were based on the grounds that plaintiff was entitled to an additional deduction on her 1947 income tax return in the amount of \$18,750.00, which was plaintiff's share of said \$75,000.00 partnership loss. A copy of said original claim, marked Exhibit Q, and a copy of said amended claim, marked Exhibit R, is attached hereto, and is incorporated by reference.

### III.

The Commissioner of Internal Revenue, through the office of the Regional Commissioner of Internal Revenue, notified plaintiff on September 10, 1954 that said \$18,750.00 chargeable loss was a 1947 loss but that in his opinion said loss was a non-business bad debt and was therefore a capital loss and thus was deductible by petitioner in 1947 only in the amount of \$1,000.00.

### IV.

Subsequently the amount of \$211.22 was refunded to plaintiff of said \$605.61 on the basis said loss was a capital loss and the balance of said claim in the amount of \$394.39 was disallowed.

### V.

Said disallowance of \$394.39 was wrongful, erroneous, and illegal in that said loss of \$18,750.00 was either a business bad debt, a loss incurred in the

business of producing motion pictures, or a joint venture loss in the business of producing a motion picture, to wit, Copacabana, and therefore deductible in full by plaintiff.

## VI.

No part of said sum of \$394.39 erroneously retained by defendant has been repaid or refunded, and said sum together with interest thereon as provided by law is due, unpaid, and owing to plaintiff from defendant.

## Tenth Count

### I.

Plaintiff, Rebecca Koch Abel, incorporates in this tenth count, all the allegations contained in Paragraphs I to IX inclusively of the first count with the same force and effect as though fully set forth herein.

### II.

In connection with her 1945 income tax return, plaintiff duly paid the income tax shown to be due by said return, to wit, the sum of \$24,779.04.

### III.

Plaintiff incurred a net operating loss for the calendar year 1947 in the amount of \$17,560.46 which loss is allowable as a net operating loss deduction carryback for the calendar year 1945.

### IV.

On or about January 7, 1949, plaintiff duly filed with the United States Collector of Internal Reve-

claim for refund in the amount of \$605.61, and on March 15, 1951, plaintiff filed an amended claim for refund for said \$605.61 in connection with her 1947 income tax return which represented all of the income tax paid by plaintiff on the said return; said claims were based on the grounds that plaintiff was entitled to an additional deduction on her 1947 income tax return in the amount of \$18,750.00, which was plaintiff's share of said \$75,000.00 partnership loss. A copy of said original claim, marked Exhibit Q, and a copy of said amended claim, marked Exhibit R, is attached hereto, and is incorporated by reference.

### III.

The Commissioner of Internal Revenue, through the office of the Regional Commissioner of Internal Revenue, notified plaintiff on September 10, 1954 that said \$18,750.00 chargeable loss was a 1947 loss but that in his opinion said loss was a non-business bad debt and was therefore a capital loss and thus was deductible by petitioner in 1947 only in the amount of \$1,000.00.

### IV.

Subsequently the amount of \$211.22 was refunded to plaintiff of said \$605.61 on the basis said loss was a capital loss and the balance of said claim in the amount of \$394.39 was disallowed.

### V.

Said disallowance of \$394.39 was wrongful, erroneous, and illegal in that said loss of \$18,750.00 was either a business bad debt, a loss incurred in the



business of producing motion pictures, or a joint venture loss in the business of producing a motion picture, to wit, Copacabana, and therefore deductible in full by plaintiff.

## VI.

No part of said sum of \$394.39 erroneously retained by defendant has been repaid or refunded, and said sum together with interest thereon as provided by law is due, unpaid, and owing to plaintiff from defendant.

## Tenth Count

### I.

Plaintiff, Rebecca Koch Abel, incorporates in this tenth count, all the allegations contained in Paragraphs I to IX inclusively of the first count with the same force and effect as though fully set forth herein.

### II.

In connection with her 1945 income tax return, plaintiff duly paid the income tax shown to be due by said return, to wit, the sum of \$24,779.04.

### III.

Plaintiff incurred a net operating loss for the calendar year 1947 in the amount of \$17,560.46 which loss is allowable as a net operating loss deduction carryback for the calendar year 1945.

### IV.

On or about January 7, 1949, plaintiff duly filed with the United States Collector of Internal Reve-

nue for the First District of California, an original claim for refund in the amount of \$12,142.17 in connection with said 1945 income tax return, and on March 15, 1951, plaintiff filed an amended claim for refund in the same amount of \$12,142.17. Said claims were based on the ground that plaintiff was entitled to a net operating loss deduction of \$17,560.46 for said year and in particular that plaintiff's \$18,750.00 chargeable share of the aforementioned \$75,000.00 loss was a loss from the operation of a business regularly carried on by said H. Koch & Sons. A copy of said original claim, marked Exhibit S, and a copy of said amended claim, marked Exhibit T, is attached hereto, and is incorporated by reference.

#### V.

The Commissioner of Internal Revenue, through the Office of the Regional Commissioner of Internal Revenue, notified plaintiff on September 10, 1954, that his ruling was that said \$75,000.00 loss was a non-business loss and that therefore plaintiff could not include his share of said loss in a net operating loss. Said claims for refund were therefore denied.

#### VI.

Said disallowance of said claims for refund was wrongful, erroneous, and illegal in that said \$75,000.00 loss and plaintiff's share of same was either a business bad debt, a loss incurred in the business of producing motion pictures, or a joint venture loss in the business of producing a motion picture, to

wit, Copacabana, and in any case constituted a loss from a business regularly carried on by H. Koch & Sons and therefore by plaintiff.

## VII.

No part of said sum of \$12,142.17 erroneously retained by defendant has been repaid or refunded, and said sum together with interest thereon as provided by law is due, payable and owing to plaintiff from defendant.

## Eleventh Count

Comes Now Plaintiff, Maurice P. Koch, and for an Eleventh Cause of Action Against the Defendant Alleges That:

### I.

Plaintiff, Maurice P. Koch, incorporates in this eleventh count, all the allegations contained in Paragraphs I to IX inclusively of the first count with the same force and effect as though fully set forth herein.

### II.

In addition, plaintiff advanced in behalf of Beacon Pictures Corporation \$15,000.00 from the community funds of his wife and himself upon the same basis that said aforementioned \$75,000.00 was advanced. Said \$15,000.00 was also lost in 1947.

### III.

Plaintiff and his wife, Daisy Koch, filed separate returns for the year 1947, and did not claim any

portion of said \$18,750.00 chargeable loss and said \$15,000.00 loss on said returns.

#### IV.

On or about January 7, 1949, plaintiff duly filed with the United States Collector of Internal Revenue for the First District of California, an original claim for refund in the amount of \$860.52 and on March 15, 1951, plaintiff filed an amended claim for refund for said \$860.52 in connection with his 1947 income tax return which represented all of the income tax paid by plaintiff on said return; said claims were based on the grounds that plaintiff was entitled to an additional deduction on his 1947 income tax return of \$16,875.00 which was plaintiff's one-half community share of his \$18,750.00 chargeable loss on the aforementioned \$75,000.00 loss or \$9,375.00, and his one-half community share of the aforementioned \$15,000.00 loss or \$7,500.00. A copy of said original claim, marked Exhibit U and a copy of said amended claim, marked Exhibit V, is attached hereto, and is incorporated by reference.

#### V.

The Commissioner of Internal Revenue, through the office of the Regional Commissioner of Internal Revenue, notified plaintiff on September 10, 1954, that said \$16,875.00 loss was a 1947 loss but that in his opinion said loss was a non-business bad debt and was therefore a capital loss and thus was deductible by petitioner in 1947 only in the amount of \$1,000.00.

## VI.

Subsequently said claim for refund in the amount of \$860.52 was disallowed.

## VII.

Said disallowance of the claim for refund was wrongful, erroneous, and illegal in that said loss of \$9,375.00 and said loss of \$7,500.00 were either business bad debts, losses incurred in the business of producing motion pictures, or joint venture losses in the business of producing a motion picture, to wit, Copacabana, and therefore deductible in full by plaintiff.

## VIII.

No part of said sum of \$860.52 erroneously retained by defendant has been repaid or refunded, and said sum together with interest thereon as provided by law is due, unpaid, and owing to plaintiff from defendant.

## Twelfth Count

## I.

Plaintiff, Maurice P. Koch, incorporates in this twelfth count, all the allegations contained in Paragraphs I to IX inclusively of the first count with the same force and effect as though fully set forth herein.

## II.

Plaintiff incorporates all the allegations contained in Paragraph II of the eleventh count with the same force and effect as though fully set forth herein.

## III.

In connection with his 1945 income tax return, plaintiff duly paid the income tax shown to be due by said return, to wit, the sum of \$8,993.04.

## IV.

Plaintiff incurred a net operating loss for the calendar year 1947 in the amount of \$8,666.79 which loss is allowable as a net operating loss deduction carryback for the calendar year 1945.

## V.

On or about January 7, 1949, plaintiff duly filed with the United States Collector of Internal Revenue for the First District of California, an original claim for refund in the amount of \$4,649.77 in connection with said 1945 income tax return, and on March 15, 1951, plaintiff filed an amended claim for refund in the same amount of \$4,649.77. Said claims were based on the ground that plaintiff was entitled to a net operating loss deduction of \$8,666.79 for said year and in particular that plaintiff's \$18,750.00 chargeable share of the aforementioned \$75,000.00 loss and said aforementioned \$15,000.00 loss were losses from the operation of a business regularly carried on by said H. Koch & Sons and by plaintiff. A copy of said original claim, marked Exhibit W, and a copy of said amended claim, marked Exhibit X, is attached hereto, and is incorporated by reference.

## VI.

The Commissioner of Internal Revenue, through

the Office of the Regional Commissioner of Internal Revenue, notified plaintiff on September 10, 1954, that his ruling was that said \$75,000.00 loss and said \$15,000.00 loss were non-business losses and that therefore plaintiff could not include his share of said losses in a net operating loss. Said claims for refund were therefore denied.

### VII.

Said disallowance of said claims for refund was wrongful, erroneous, and illegal in that said \$75,000.00 loss and plaintiff's share of same and said \$15,000.00 loss were either business bad debts, losses incurred in the business of producing motion pictures, or a joint venture loss in the business of producing a motion picture, to wit, Copacabana, and in any case constituted losses from a business regularly carried on by H. Koch & Sons and by plaintiff.

### VIII.

No part of said \$4,649.77 erroneously retained by defendant has been repaid or refunded, and said sum together with interest thereon as provided by law is due, payable and owing to plaintiff from defendant.

### Thirteenth Count

Comes Now Plaintiff, Daisy Koch, and for a Thirteenth Cause of Action Against the Defendant Alleges That:

#### I.

Plaintiff, Daisy Koch, incorporates in this thirteenth count, all the allegations contained in Para-

graphs I to IX inclusively of the first count with the same force and effect as though fully set forth herein.

## II.

In addition, plaintiff's husband, Maurice P. Koch advanced in behalf of Beacon Pictures Corporation \$15,000.00 from the community funds of plaintiff and himself upon the same basis that said aforementioned \$75,000.00 was advanced. Said \$15,000.00 was also lost in 1947.

## III.

Plaintiff and her husband filed separate returns for the year 1947, and did not claim any portion of said \$18,750.00 chargeable loss and said \$15,000.00 loss on said returns.

## IV.

On or about January 7, 1949, plaintiff duly filed with the United States Collector of Internal Revenue for the First District of California, an original claim for refund in the amount of \$860.53 and on March 15, 1951, plaintiff filed an amended claim for refund for said \$860.53 in connection with said return; said claims were based on the grounds that plaintiff was entitled to an additional deduction on her 1947 income tax return of \$16,875.00 which was plaintiff's one-half community share of her husband's \$18,750.00 chargeable loss on the aforementioned \$75,000.00 loss or \$9,375.00, and her one-half community share of the aforementioned \$15,000.00 loss or \$7,500.00. A copy of said original claim, marked Exhibit Y and a copy of said amended



claim, marked Exhibit Z, is attached hereto, and is incorporated by reference.

### V.

The Commissioner of Internal Revenue, through the office of the Regional Commissioner of Internal Revenue, notified plaintiff on September 10, 1954, that said \$16,875.00 loss was a 1947 loss but that in his opinion said loss was a non-business bad debt and was therefore a capital loss and thus was deductible by petitioner in 1947 only in the amount of \$1,000.00.

### VI.

Subsequently, said claim for refund in the amount of \$860.53 was disallowed.

### VII.

Said disallowance of the claim for refund was wrongful, erroneous, and illegal in that said loss of \$9,375.00 and said loss of \$7,500.00 were either business bad debts, losses incurred in the business of producing motion pictures, or joint venture losses in the business of producing a motion picture, to wit, Copacabana, and therefore deductible in full by plaintiff.

### VIII.

No part of said sum of \$860.53 erroneously retained by defendant has been repaid or refunded, and said sum together with interest thereon as provided by law is due, unpaid, and owing to plaintiff from defendant.

## Fourteenth Count

## I.

Plaintiff, Daisy Koch, incorporates in this fourteenth count, all the allegations contained in Paragraphs I to IX inclusively of the first count with the same force and effect as though fully set forth herein.

## II.

Plaintiff incorporates all the allegations contained in Paragraph II of the thirteenth count with the same force and effect as though fully set forth herein.

## III.

In connection with her 1945 income tax return, plaintiff duly paid the income tax shown to be due by said return, to wit, the sum of \$9,579.13.

## IV.

Plaintiff incurred a net operating loss for the calendar year 1947 in the amount of \$8,666.78 which loss is allowable as a net operating loss deduction carryback for the calendar year 1945.

## V.

On or about January 7, 1949, plaintiff duly filed with the United States Collector of Internal Revenue for the First District of California, an original claim for refund in the amount of \$4,797.74 in connection with said 1945 income tax return, and on March 15, 1951, plaintiff filed an amended claim for refund in the same amount of \$4,797.74. Said claims

were based on the ground that plaintiff was entitled to a net operating loss deduction of \$8,666.78 for said year and in particular that plaintiff's one-half community share of her husband's \$18,750.00 share of the aforementioned \$75,000.00 partnership loss and plaintiff's one-half community share of said aforementioned \$15,000.00 loss were losses from the operation of a business regularly carried on by H. Koch & Sons and by plaintiff's husband. A copy of said original claim, marked Exhibit AA and a copy of said amended claim, marked Exhibit BB, is attached hereto, and is incorporated by reference.

#### VI.

The Commissioner of Internal Revenue, through the office of the Regional Commissioner of Internal Revenue, notified plaintiff on September 10, 1954, that his ruling was that said \$75,000.00 loss and said \$15,000.00 loss were non-business losses and that therefore plaintiff could not include her share of said losses in a net operating loss. Said claims for refund were therefore denied.

#### VII.

Said disallowance of said claims for refund was wrongful, erroneous, and illegal in that said \$75,000.00 loss and plaintiff's husband's share of same and said \$15,000.00 loss were either business bad debts, losses incurred in the business of producing motion pictures, or a joint venture loss in the business of producing a motion picture, to wit, Copacabana, and in any case constituted losses from a

business regularly carried on by H. Koch & Sons and by plaintiff.

### VIII.

No part of said \$4,649.77 erroneously retained by defendant has been repaid or refunded, and said sum together with interest thereon as provided by law is due, payable and owing to plaintiff from defendant.

Wherefore, plaintiff, Harold M. Koch, demands judgment against defendant in the sum of \$3,739.90 together with interest according to law on said overpaid taxes, together with plaintiff's costs of suit herein, and for such other and further relief as the Court may find meet and just in the premises.

Wherefore, plaintiff, Bessie Koch, demands judgment against defendant in the sum of \$3,884.08 together with interest according to law on said overpaid taxes, together with plaintiff's costs of suit herein, and for such other and further relief as the Court may find meet and just in the premises.

Wherefore, plaintiff, William L. Koch, demands judgment against defendant in the sum of \$3,739.90 together with interest according to law on said overpaid taxes, together with plaintiff's costs of suit herein, and for such other and further relief as the Court may find meet and just in the premises.

Wherefore, plaintiff, Rose Koch, demands judgment against defendant in the sum of \$3,884.08 together with interest according to law on said overpaid taxes, together with plaintiff's costs of suit

herein, and for such other and further relief as the Court may find meet and just in the premises.

Wherefore, plaintiff, Rebecca Koch Abel, demands judgment against defendant in the sum of \$12,536.56 together with interest according to law on said overpaid taxes, together with plaintiff's costs of suit herein, and for such other and further relief as the Court may find meet and just in the premises.

Wherefore, plaintiff, Maurice P. Koch, demands judgment against defendant in the sum of \$5,510.29 together with interest according to law on said overpaid taxes, together with plaintiff's costs of suit herein, and for such other and further relief as the Court may find meet and just in the premises.

Wherefore, plaintiff, Daisy Koch, demands judgment against defendant in the sum of \$5,658.27 together with interest according to law on said overpaid taxes, together with plaintiff's costs of suit herein, and for such other and further relief as the Court may find meet and just in the premises.

/s/ LEON SCHILLER.

We hereby request and demand a trial by jury on all counts of this complaint.

/s/ LEON SCHILLER.

[Endorsed]: Filed July 5, 1955.

[Title of District Court and Cause.]

### ANSWER

The defendant, United States of America, by its attorney, Lloyd H. Burke, United States Attorney, in and for the Northern District of California, for its answer to plaintiffs' complaint, admits, denies and alleges as follows:

#### First Count

1. Admits the allegations of Paragraph I, except to deny that any taxes were erroneously, illegally or wrongfully assessed or collected.

2. Admits, except to deny the allegations or implications that plaintiffs duly and correctly reported income, and except to deny the implication or allegation that plaintiffs are entitled to recover any taxes.

3. Defendant is without information sufficient to form a belief as to the truth of the allegations contained in Paragraph III, except to admit that partnership tax returns were filed for the alleged partnership showing the alleged persons as partners for the years 1945, 1946 and 1947.

4. Denies, except to admit that the alleged partnership was engaged in business of luggage manufacturing. Further answering Paragraph IV, defendant says that the alleged partnership in its 1945, 1946 and 1947, and amended 1947 tax returns

reported its business as only luggage manufacturing.

5. Defendant is without information sufficient to form a belief as to the truth of the allegations contained in Paragraph V, except as hereinafter admitted or denied. Further answering Paragraph V, defendant alleges that in August, 1946, a corporation named Beacon Picture Corporation was in existence and existed for the purpose of making a motion picture entitled Copacabana. In 1946, the alleged partnership, H. Koch & Sons, loaned \$75,000 to said Beacon Pictures Corporation. Defendant denies that this \$75,000 was loaned in connection with the joint venture and denies that any joint venture existed. Defendant admits that the alleged partnership, H. Koch & Sons, acquired an interest in said motion picture which interest entitled it to a share of profits from said production. Said interest was in the nature of additional compensation for the use of said \$75,000 and was granted as an inducement to enter into the loan. Defendant denies that the \$75,000 would be repaid only if the undertaking was successful.

6. Admits, except to deny the allegation or implication that the transfer of said \$75,000 was anything other than a loan.

7. Defendant is without information sufficient to form a belief as to the truth of allegations contained in Paragraph VII, except that defendant admits that the partnership return claimed no \$75,000 loss.

8. Denies, except to admit that the original partnership return reported ordinary net income of \$19,223.18.

9. Defendant has no information sufficient to form a belief as to the truth of the allegations contained in Paragraph IX.

10. Admits, except to deny that plaintiff, Harold M. Koch, and his wife, Bessie Koch, were entitled to a deduction of \$18,750.00.

11. Denies, except to admit that plaintiff filed claims for refund for the amounts alleged. Defendant says the original claim was filed on June 23, 1949, and the amended claim on March 15, 1951.

12. Denies, except to admit that on September 10, 1954, defendant or its agent notified plaintiff that his claim for refund could not be allowed because it had been ruled that the alleged loss was a non-business bad debt.

13. Denies. Defendant says that the amount of \$149.12 was refunded to plaintiff, \$42.12 of which represented interest.

14. Denies.

15. Denies.

### Second Count

1. Defendant, United States of America, incorporates in this Count its answers to Paragraphs I to X, inclusive, of the First Count with the same force and effect as though set forth herein.



2. Admits, except to deny plaintiff paid the full tax due for the year 1945.

3. Denies.

4. Denies, except to admit plaintiff filed claims for refund in the amounts alleged. Defendant says the original claim was filed on June 23, 1949, and the amended claim on March 15, 1951.

5. Denies, except to admit that on September 10, 1954, defendant or its agent notified plaintiff that his claim for refund could not be allowed because it had been ruled that the alleged loss was a non-business bad debt.

6. Denies.

7. Denies.

### Third Count

1. Defendant, United States of America, incorporates in this Third Count its answers to Paragraphs I to IX, inclusive, of the First Count with the same force and effect as though set forth at length herein.

2. Admits, except to deny that plaintiff, Bessie Koch, or her husband, Harold Koch, were entitled to a deduction of \$18,750.00.

3. Denies, except to admit that plaintiff filed claims for refund for the amounts alleged. Defendant says the original claim was filed on June 23, 1949, and the amended claim on March 15, 1951.

4. Denies, except to admit that on September 10, 1954, defendant or its agent notified plaintiff

that her claim for refund could not be allowed because it had been ruled that the alleged loss was a non-business bad debt.

5. Denies. Defendant says that the amount of \$149.12 was refunded, \$42.12 of which represented interest.

6. Denies.

7. Denies.

#### Fourth Count

1. Defendant, United States of America, incorporates in this Fourth Count its answers to Paragraphs I to IX, inclusive, of the First Count with the same force and effect as though set forth at length herein.

2. Admits, except to deny that plaintiff paid the full tax due for the year 1945.

3. Denies.

4. Denies, except to admit that plaintiff filed claims for refund for the amounts alleged. Defendant says the original claim was filed on June 23, 1949, and the amended claim on March 15, 1951.

5. Denies, except to admit that on September 10, 1954, defendant or its agent notified plaintiff that her claim for refund could not be allowed because it had been ruled that the alleged loss was a non-business bad debt.

6. Denies.

7. Denies.

Fifth Count

1. Defendant, United States of America, incorporates in its Fifth Count its answers to Paragraphs I to IX, inclusive, of the First Count with the same force and effect as though set forth at length herein.

2. Admits, except to deny that plaintiff, William L. Koch, or his wife, Rose Koch, were entitled to a deduction of \$18,750.

3. Denies, except to admit that plaintiff filed claims for refund for the amounts alleged. Defendant says the original claim was filed on June 23, 1949, and the amended claim on March 15, 1951.

4. Denies, except to admit that on September 10, 1954, defendant or its agent notified plaintiff that his claim for refund could not be allowed because it had been ruled that the alleged loss was a non-business debt.

5. Denies. Defendant says that the amount of \$149.12 was refunded to plaintiff, \$42.12 of which represented interest.

6. Denies.

7. Denies.

Sixth Count

1. Defendant, United States of America, incorporates in this Sixth Count its answers to Paragraphs I to IX, inclusive, of the First Count with the same force and effect as though set forth at length herein.

2. Admits, except to deny that plaintiff paid in full the tax due for the year 1945.

3. Denies.

4. Denies, except to admit that plaintiff filed claims for refund for the amounts alleged. Defendant says that the original claim was filed on June 23, 1949, and the amended claim on March 15, 1951.

5. Denies, except to admit that on September 10, 1954, defendant or its agent notified plaintiff that his claim for refund could not be allowed because it had been ruled that the alleged loss was a non-business bad debt.

6. Denies.

7. Denies.

#### Seventh Count

1. Defendant, United States of America, incorporates in this Seventh Count its answers to Paragraphs I to IX, inclusive, of the First Count with the same force and effect as though set forth at length herein.

2. Admits, except to deny that plaintiff, Rose Koch, or her husband, William L. Koch, were entitled to deduction of \$18,750 for 1945 or for 1947. Further answering Paragraph II defendant says that plaintiff and her husband also filed separate returns for the year 1947.

3. Denies, except to admit that plaintiff filed claims for refund for the amounts alleged. Defend-

ant says the original claim was filed on June 23, 1949, and the amended claim on March 15, 1951.

4. Denies, except to admit that on September 10, 1951, defendant or its agent notified plaintiff that her claim for refund could not be allowed because it had been ruled that the alleged loss was a non-business bad debt.

5. Denies. Defendant says that the amount of \$149.12 was refunded to plaintiff, \$42.12 of which represented interest.

6. Denies.

7. Denies.

#### Eighth Count

1. The defendant, United States of America, incorporates in this Eighth Count its answers to the allegations contained in Paragraphs I to IX, inclusive, of the First Count with the same force and effect as though set forth at length herein.

2. Admits, except to deny plaintiff paid the full tax due for 1945.

3. Denies.

4. Denies, except to admit that plaintiff filed claims for refund for approximately the amounts alleged. Defendant says that each claim was for refund of \$3,673.09. Defendant says the original claim was filed on June 23, 1949, and the amended claim on March 15, 1951.

5. Denies, except to admit that on September 10, 1954, defendant or its agent notified plaintiff that her claim for refund could not be allowed because it had been ruled that the alleged loss was a non-business bad debt.

6. Denies.

7. Denies.

### Ninth Count

1. Defendant, United States of America, incorporates in this Ninth Count its answers to the allegations contained in Paragraph I and Paragraphs III through IX, inclusive, of the First Count with the same force and effect as though set forth at length herein.

With respect to Paragraph II of the First Count, defendant admits the allegations contained therein, except to deny the allegations or implications that she duly and correctly reported her income and except to deny the allegations or implications that plaintiff is entitled to recover any taxes and except that the defendant has no knowledge or information sufficient to form a belief as to the truth of the allegation that plaintiff resides in San Francisco, California.

2. Denies, except to admit that plaintiff filed an original and amended claims for refund of \$605.61 for 1947 income taxes on June 23, 1949, and March 15, 1951, respectively.

3. Defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph III.

4. Defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph IV.

5. Denies.

6. Denies.

#### Tenth Count

1. The defendant, United States of America, incorporates in this Tenth Count its answer to Paragraph I of the Ninth Count with the same force and effect as though set forth at length herein.

2. Admits, except to deny that plaintiff paid the full tax due for 1945.

3. Denies.

4. Denies, except to admit that plaintiff filed claims for refund for the amounts alleged. Defendant says the original claim was filed on June 23, 1949, and the amended claim on March 15, 1951.

5. The defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph V.

6. Denies.

7. Denies.

#### Eleventh Count

1. The defendant, United States of America, incorporates in this Eleventh Count its answers to

the allegations contained in Paragraphs I to IX inclusive, of the First Count with the same force and effect as though set forth at length herein.

2. Admits, except to deny that this transaction was other than a loan and except to deny that the basis of this loan was the same as the basis of the \$75,000 loan.

3. Admits, except to deny that plaintiff, Maurice P. Koch, or his wife, Daisy Koch, were entitled to deductions of \$18,750 or \$15,000 and except to deny that plaintiff suffered a "chargeable" loss in either of these amounts.

4. Denies, except to admit that plaintiff filed claims for refund for the amounts alleged. Defendant says the original claim was filed on June 23, 1949, and the amended claim on March 15, 1951.

5. Denies, except to admit that on September 10, 1954, defendant or its agent notified plaintiff that his claim for refund could not be allowed because it had been ruled that the alleged loss was a non-business bad debt.

6. Denies.

7. Denies.

8. Denies.

#### Twelfth Count

1. The defendant, United States of America incorporates in this Twelfth Count its answers to the allegations contained in Paragraphs I to IX



inclusive, of the First Count with the same force and effect as though set forth at length herein.

2. The defendant, United States of America, incorporates in this Twelfth Count its answer to the allegations contained in Paragraph II of the Eleventh Count with the same force and effect as though set forth at length herein.

3. Admits, except to deny that plaintiff paid in full taxes due for the year 1945.

4. Denies.

5. Denies, except to admit that plaintiff filed claims for refund for the amounts alleged. Defendant says the original claim was filed on June 23, 1949, and the amended claim on March 15, 1951.

6. Denies, except to admit that on September 10, 1954, defendant or its agent notified plaintiff that his claim for refund could not be allowed because it had been ruled that the alleged loss was a non-business bad debt.

7. Denies.

8. Denies.

### Thirteenth Count

1. The defendant, United States of America, incorporates in this Thirteenth Count its answers to the allegations contained in Paragraphs I to IX, inclusive, of the First Count with the same force and effect as though set forth at length herein.

2. Admits, except to deny that this transaction was other than a loan and except to deny that the basis of this loan was the same as the basis of the \$75,000 loan.

3. Admits, except to deny that plaintiff or her husband was entitled to deductions of \$18,750 or \$15,000 and except to deny that plaintiff suffered a "chargeable" loss on either of these amounts.

4. Denies, except to admit that plaintiff filed claims for refund for amounts alleged. Defendant says the original claim was filed June 23, 1949, and the amended claim on March 15, 1951.

5. Denies, except to admit that on September 10, 1954, defendant or its agent notified plaintiff that her claim for refund could not be allowed because it had been ruled that the alleged loss was a non-business bad debt.

6. Denies.

7. Denies.

8. Denies.

#### Fourteenth Count

1. The defendant, United States of America, incorporates in this Fourteenth Count its answers to the allegations contained in Paragraphs I to IX, inclusive, of the First Count with the same force and effect as though set forth at length herein.

2. The defendant, the United States of America, incorporates, in this Fourteenth Count its answer to the allegations contained in Paragraph II of the

Thirteenth Count with the same force and effect as though set forth at length herein.

3. Admits, except to deny that plaintiff paid the full taxes due for the year 1945.

4. Denies.

5. Denies, except to admit that plaintiff filed claims for refund for the amounts alleged. Defendant says the original claim was filed on June 23, 1949, and the amended claim on March 15, 1951.

6. Denies, except to admit that on September 10, 1954, defendant or its agent notified plaintiff that her claim for refund could not be allowed because it had been ruled that the alleged loss was a non-business bad debt.

7. Denies.

8. Denies.

#### Partial Affirmative Defense

Plaintiffs have not calculated correctly the amount of refund due under their theory.

Wherefore, having fully answered, defendant prays for dismissal of plaintiffs' complaint, for judgment in its favor, for costs and for such other relief as may be just and proper.

/s/ LLOYD H. BURKE,

By /s/ LYNN J. GILLARD,

United States Attorney.

Affidavit of service by mail attached.

[Endorsed]: Filed October 24, 1955.

[Endorsed]: No. 15645. United States Court of Appeals for the Ninth Circuit. Harold M. Koch, Bessie Koch, William L. Koch, Rose Koch, Rebecca Koch Abel, Maurice P. Koch, and Daisy Koch, Appellants, vs. United States of America, Appellee. Supplemental Transcript of Record. Appeal from the United States District Court for the Northern District of California, Southern Division.

Filed: July 17, 1957.

Docketed: July 27, 1957.

/s/ PAUL P. O'BRIEN,  
Clerk of the United States Court of Appeals for  
the Ninth Circuit.

No. 15,645

United States Court of Appeals  
For the Ninth Circuit

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HAROLD M. KOCH, BESSIE KOCH, WIL-  
LIAM L. KOCH, ROSE KOCH, REBECCA  
KOCH ABEL, MAURICE P. KOCH, and  
DAISY KOCH,

*Appellants,*

VS.

UNITED STATES OF AMERICA,

*Appellee.*

On Appeal from the United States District Court  
for the Northern District of California.

APPELLANTS' PETITION FOR A REHEARING.

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MAX FINK,

LEON SCHILLER,

105 Montgomery Street,

San Francisco 4, California,

*Attorneys for Appellants  
and Petitioners.*

FILED

OCT 10 1958

PAUL P. O'BRIEN, CL

[Endorsed]: No. 15645. United States Court of Appeals for the Ninth Circuit. Harold M. Koch, Bessie Koch, William L. Koch, Rose Koch, Rebecca Koch Abel, Maurice P. Koch, and Daisy Koch, Appellants, vs. United States of America, Appellee. Supplemental Transcript of Record. Appeal from the United States District Court for the Northern District of California, Southern Division.

Filed: July 17, 1957.

Docketed: July 27, 1957.

/s/ PAUL P. O'BRIEN,  
Clerk of the United States Court of Appeals for  
the Ninth Circuit.

No. 15,645

United States Court of Appeals  
For the Ninth Circuit

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HAROLD M. KOCH, BESSIE KOCH, WIL-  
LIAM L. KOCH, ROSE KOCH, REBECCA  
KOCH ABEL, MAURICE P. KOCH, and  
DAISY KOCH,

*Appellants,*

VS.

UNITED STATES OF AMERICA,

*Appellee.*

On Appeal from the United States District Court  
for the Northern District of California.

APPELLANTS' PETITION FOR A REHEARING.

---

MAX FINK,

LEON SCHILLER,

105 Montgomery Street,

San Francisco 4, California,

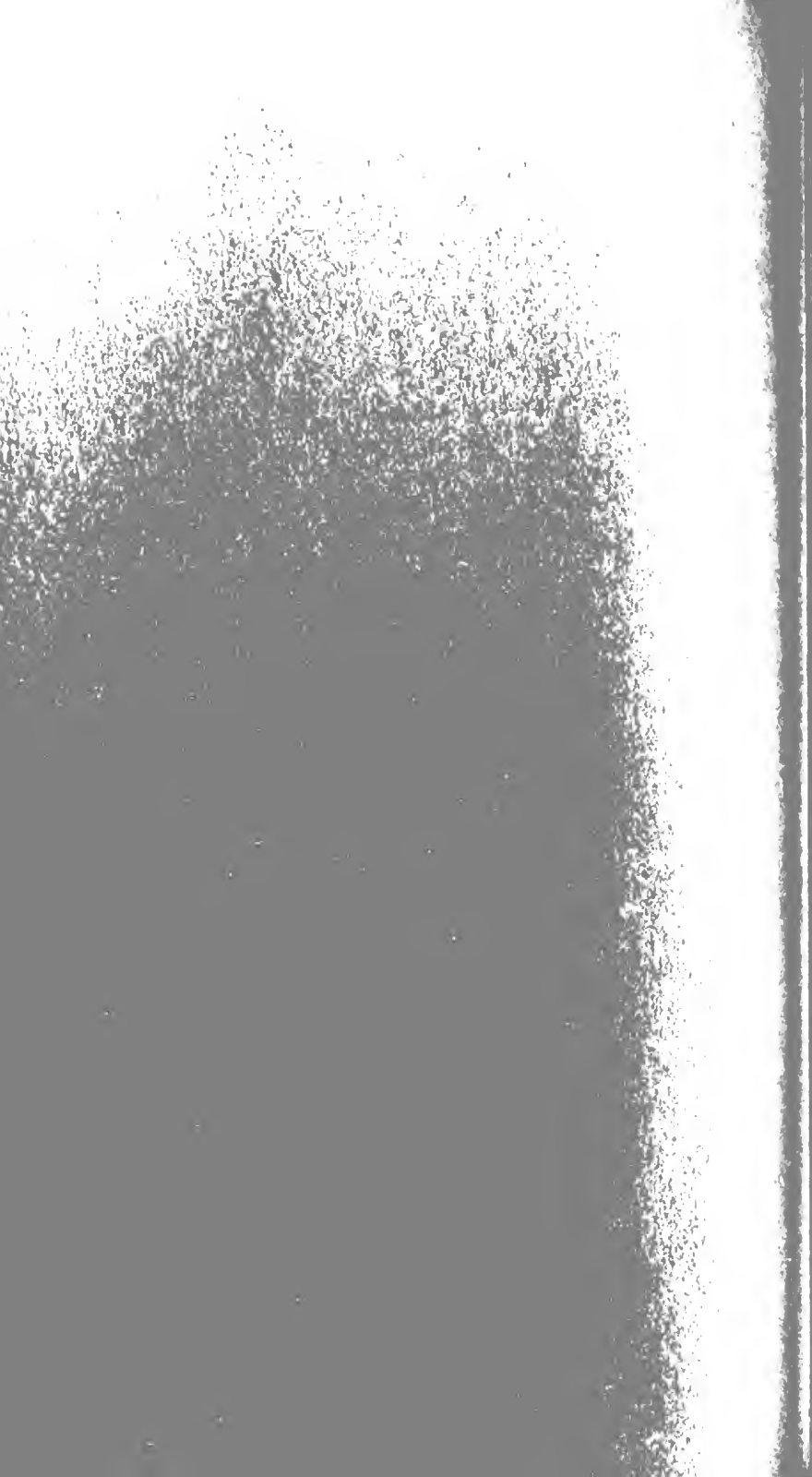
*Attorneys for Appellants*

*and Petitioners.*

FILED

OCT 10 1958

PAUL P. O'BRIEN, CL





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SECRET

# United States Court of Appeals

For the Ninth Circuit

San Francisco, California

Before the Honorable Chief Judge and Honorable Judges of the Court

Appeals from the United States District Court for the District of

San Francisco, California

Filed for the Plaintiff

and for the Defendant

in the case of

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**United States Court of Appeals  
For the Ninth Circuit**

HAROLD M. KOCH, BESSIE KOCH, WIL-  
LIAM L. KOCH, ROSE KOCH, REBECCA  
KOCH ABEL, MAURICE P. KOCH, and  
DAISY KOCH,

*Appellants,*

VS.

UNITED STATES OF AMERICA,

*Appellee.*

**On Appeal from the United States District Court  
for the Northern District of California.**

**APPELLANTS' PETITION FOR A REHEARING.**

*To the Honorable Judges of the United States Court  
of Appeals for the Ninth Circuit:*

Appellants, on the grounds following, petition for a rehearing of the Court's judgment affirming the judgment of the District Court for the Northern District of California.

**I.**

**THIS HONORABLE COURT HAS OVERLOOKED A WELL SETTLED PRINCIPLE OF LAW SUPPORTED BY CONSISTENT AUTHORITIES, AND ITS OPINION THREATENS EMBARRASSMENT AND CONFUSION IN THE AUTHORITIES.**

The rule regarding the effect of the presumption of correctness of determinations by the Commissioner of

Internal Revenue in the trial of tax causes has been well settled. The presumption disappears upon the introduction of evidence, and the issues are then tried, determined and depend *wholly upon the evidence produced*. The presumption cannot be considered when weighing the evidence. The presumption is *no longer existent* after the introduction of evidence, and *cannot affect the burden of proof*. When evidence has been introduced, the cause must be decided *upon the evidence alone*.

Appellants cited established authority, and particularly the decisions of this Court, in the cases as follows:

In the case of *Hemphill Schools v. Commissioner of Internal Revenue*, 137 F. 2d 961, C.C.A. 9 (1943), at pp. 963, 964, this Honorable Court reversed and remanded the cause for trial with the direction that the trial body: "(1) Find from the evidence, and from it alone . . ."

In that case this Court stated:

"Thus, if no evidence had been produced, the Board would have had to accept the determination; for, until evidence was produced, the determination was presumed to be correct. *Evidence was produced*. Some of the evidence produced by the petitioner tended to prove that its gains and profits were not permitted to accumulate beyond the reasonable needs of its business. Evidence having been so produced, *the presumption ceased, and thenceforth the issue depended 'wholly upon the evidence.'* It thus became the duty of the Board to find *from the evidence, and from it*

*alone*, whether petitioner's gains and profits were permitted to accumulate beyond the reasonable needs of its business. No such finding was made. Instead, the Board treated the *presumption (which no longer existed) as if it were evidence, weighed it against petitioner's evidence and concluded that petitioner's evidence did not 'overcome' it.*

"Decision vacated and case remanded, with direction to (1) find from the evidence, *and from it alone*, whether petitioner's gains and profits were permitted to accumulate beyond the reasonable needs of its business." (Emphasis ours, as well as this Court's in certain instances.)

Appellants also cited this Court's decision in the case of *San Joaquin Brick Co. v. Commissioner of Internal Revenue*, 130 F. 2d 220, C.C.A. 9 (1942), at p. 225:

"But once he presents competent and relevant evidence on every necessary element, the presumption of correctness of the Commissioner's determination *is no longer existent* and the outcome of the case depends upon the determination of the trial body after the consideration of the evidence brought before it by both sides." (Emphasis ours.)

Appellants also cited this Court's decision in the case of *J. M. Perry v. Commissioner*, 120 F. 2d 123 (1941) C.C.A. 9:

"This finding is presumptively correct, that is, until the taxpayer proceeds with competent and relevant evidence to support his position, the determination of the Commissioner stands. When

such *evidence* has been adduced the issues depend *wholly* upon the evidence so adduced and the evidence to be adduced by the Commissioner. *The Commissioner cannot rely upon his determination as evidence of its correctness either directly or as affecting the burden of proof.*" (Emphasis ours.)

In *Lawrence v. Commissioner of Internal Revenue* (1944) (9th C.C.A.), 143 F. 2d 456, this Court held that the presumption disappears when evidence is introduced sufficient to establish a *prima facie* case.

On September 12, 1958, this Honorable Court filed its opinion, in contravention of all prior decisions cited, and without reviewing or considering the same, the opinion states (on the last page) as follows:

"Appellants also object to an instruction on the ground that the presumption that the administrative determination that the partnership was not engaged in a trade or business was given *too much weight*. Appellants admit that there is such a presumption but *claim* it vanishes when evidence is produced."

Thus this Court has erroneously overruled all authorities upon the subject which clearly hold that the presumption disappears completely upon the introduction of evidence, and is no longer existent following the introduction of evidence. The authorities have determined that under no circumstances may the presumption be considered as evidence when actual proofs are made; that under no circumstances may the presumption preponderate over evidence adduced during trial. All previous authority on the subject has now been discarded by this Court with the statement that

appellants "claim" such a rule, and that the matter has a relationship to the *amount* of "weight."

By its failure to approve the respectable authority upon the subject, and its erroneous view of this cause, this Honorable Court has done away with the basic concept of the trial of all tax causes. We now have injected into the field of jurisprudence and fair trial, the concept that the one who is sued may, by his own self-serving declaration, establish evidentiary values which may preponderate over actual evidence adduced during trial. Thus a rule of "going forward" has been vicariously catapulted into the realm of evidentiary values which may preponderate over actual evidence adduced during trial. See *Redfield v. Eaton* (D.C.) (1931), 53 F. 2d 693, 696, which states:

"But that the Commissioner's decision, resting on evidence not presented to the Court—in this case the defendant offered not a single witness—has the quality of probative evidence in determining the preponderance of evidence, is a proposition supported neither by authority nor reason."

In the instant cause, just as in *Redfield v. Eaton*, supra, the defendant offered not a single witness, and in fact no evidence of probative value, and rested entirely on the presumption, which in turn was based upon nebulous considerations made outside of Court.

In giving such effect to the extrajudicial determination and self-serving declaration of the Commissioner of Internal Revenue, the trial Court, and now this Honorable Court have denied to appellants due process of law and a fair trial.

In the last paragraph of its decision, this Court repeats a portion of the instruction given as follows:

“The burden is upon the plaintiff to overcome the presumption of the correctness of the Commissioner’s determination by proving by a preponderance of the evidence that they were engaged in a trade or business of financing motion pictures.”

This instruction clearly stated that the presumption affects the burden of proof; that a prima facie case is not a sufficient showing; that the presumption must be weighed with evidence opposing it; that the presumption continues during and throughout the determination and weighing of the cause and the evidence produced at trial.

The last sentence of the opinion is indeed shocking. Just prior to its appearance this Court reprints the portion of the instruction which states, in crystal-clear language, that the burden is upon plaintiffs to overcome the presumption by a preponderance of the evidence. The final sentence in the opinion nevertheless states:

“The instruction did not specifically state that the presumption was to be considered as evidence and the burden of proof of plaintiffs was correctly explained.”

We were surprised to find the quoted language in appellee’s brief, and we are now completely devastated to find it in the final words of this Honorable Court. Obviously, the instruction states that the burden is



upon the plaintiffs to overcome the presumption by evidence which preponderates over it.

This Honorable Court cannot now announce, without violence to concepts of law, that "the burden of proof of plaintiffs was correctly explained."

If this decision is permitted to remain without change, it would create chaos in the trial of tax causes, because:

(a) The clear rule enunciated by this Court on several occasions and the accepted and prevailing rule is now shrouded and overruled.

(b) Should trial Courts instruct the jury as to the "weight" to be given to the presumption, despite the previously prevailing rules that the presumption "disappears"; that it cannot "affect the burden of proof"; that "the presumption ceased"; that the issue depends *wholly* upon the evidence"; that the duty is to find "from the evidence, and from it alone"; that after the introduction of evidence the presumption "no longer existed"; that it is error to have "weighed it against petitioners' evidence"?

The Government did not call a witness, and its defense was based entirely upon the alleged presumption. Meticulous examination of the record reveals absolutely no testimony or evidence upon which a defense could be predicated in the absence of such alleged presumption.

The trial Court made its findings of fact and drew its conclusions of law based upon the erroneous concept that the presumption persisted, and ruled

throughout the trial, during argument, in its instructions, in its conclusions of law, and in its judgment, that the *presumption* persisted. The entire determination was based upon this erroneous view.

The presumption was the central issue in the case. The trial and determination of the cause was controlled by this erroneous concept.

This Court must recognize the violent effect of the last words of its decision, which states that "the burden of proof of plaintiffs was correctly explained."

It is not for the Appellate Court to determine the weight of the evidence. If we deduct from the scales the effect of the *presumption*, it is probable that the trier of facts would determine that the evidence favoring the taxpayer's position outweighs or is more convincing than the evidence opposed to it (there being none). The devastating effect of the erroneous use of the presumption when fortified by the Government's final emotional appeal "we submit to you, ladies and gentlemen, the finding of the Commissioner of Internal Revenue, who was a duly and legally appointed executive officer of the Government, sworn to administer Internal Revenue Laws . . ."; (R. 371) and the further argument (over objection) that "plaintiffs have already had one crack at the case" (R. 344), cannot be ignored by this Honorable Court. This error pervaded each and every determination in the trial Court, and set up a false barrier of such magnitude that the same could not be overcome.

**THE PARTNERSHIP AGREEMENT WAS ERRONEOUSLY  
CONSTRUED BY THIS COURT.**

The partnership agreement, construed within its four corners (appellants' opening brief appendix B), provides "The said partnership business will, . . . engage in the business of financing motion picture productions". The basic agreement (appellants' opening brief appendix A) provides . . . "all of said parties shall devote all of their time to the interest of said business and for the benefit thereof . . ." and further provides for forfeiture of the partnership interest if this provision is breached.

Although the partners could contribute disproportionate amounts, all such contributions are covered by the partnership agreement; the same are subject to disbursement under the partnership agreement; the same became assets of the partnership; the same are in each and every respect controlled by the partnership and by the partnership agreement; and each and every act of the partners in this connection is on behalf of the partnership.

This Honorable Court has misconstrued the partnership agreement and has stated "the partnership agreement seems to contemplate loans and other activities of the individual partners". This is diametrically opposed to a proper construction of the partnership agreement.

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**THE OPINION OF THIS HONORABLE COURT IS REplete WITH  
MISTAKES REGARDING THE FACTS OF RECORD.**

Most glaring is the constant repetition in the decision that the appellants were engaged in the business

of loaning money; whereas the record demonstrates that the activities were designed to promote and finance the pre-production "phases" (or the so-called "packaging") of film productions. Appellants desired to obtain as large a participation and ownership in each film venture as possible and advanced funds only to the extent necessary to obtain such interests. Their activities were limited to so-called "front money" (R. 226, 227) for the purpose of forming the corporation and acquiring the rights to literary properties, artistic talents and facilities (R. 40, 42, 196, 226, 227, 229, 230). They did not finance production during principal photography of films. Their efforts were devoted to assembling the corporate vehicle, stories, artistic talent, facilities and other funds necessary to production. The decision erroneously recites and repeats that they were trying to make loans.

Their continuous expenditures of valuable time, money and effort is now erroneously described in the opinion as follows: "The record is replete with activities of Maurice P. Koch consisting of telephone calls, conversations, discussions and airplane journeys"; and the opinion also states: ". . . we do not think the jury could conclude that a number of futile transactions and activities looking toward consummation of loans had *any value* in determining whether the partnership was engaged in the business of financing." (Emphasis ours.)

We are constrained to observe that this Court has knowledge of the difficulties inherent in "packaging" artistic talents, facilities and the enormous sums re-

quired for production of films, and the inherent requirements of time, energy and funds to the purpose of bringing about a merger, at the same time, of all the necessary ingredients to the production of a major motion picture in the so-called "independent" field.

Also in error is the statement: "Sebastian and Hersch repaid the \$10,000 loaned upon the sale of the first picture". This \$10,000 was not loaned; it was not repaid; and it was lost. This error in the concept of facts indicates complete misunderstanding by this Court of the facts of this case. The sum of \$15,000 was delivered by appellants to David Sebastian. \$5,000 of this sum was used by Sebastian on behalf of appellants for the expenses of organizing the affairs of Beacon Pictures. \$10,000 of this sum was used to buy the stock of Beacon Pictures in the name of one Coslow, which stock had to be in Coslow's name in order to obtain distribution through United Artists (Plaintiffs' No. 5 for identification, appendix D, appellants' opening brief) (R. 50-53, 250-252). Said Exhibit 5 was erroneously excluded by the trial Court. The opinion should correctly recite that appellants caused Beacon Pictures to be organized, and caused its properties, talents and facilities to be assembled, and that appellants expended sums for that purpose in addition to their efforts.

Despite the fact that the partnership put up the money and did everything to get this project started, the opinion recites erroneously "... but the partnership did not engage in the organization of such corporation" (Beacon).

Obviously, the \$10,000 in capital stock issued to Sam Coslow did not establish capital of any meaning when considered in the light of obligations totaling \$1,400,000.00 incurred in the production of the film. The opinion should clarify that the amounts advanced as so-called "loans", were in reality funds which could only be realized, if at all, from the success of the venture or syndicate.

This Court has also overlooked the fact that appellants were engaged in the business of "packaging" film productions for more than three years prior to the year in question, and continued to engage in the same for some years following the year in question. The opinion overlooks the salient fact that all of plaintiffs' available funds became frozen in the year 1947 in the unfortunate film called Copacabana, and that the freezing and loss of these funds prevented the conclusion of the many pending negotiations. The opinion is also erroneous in concluding that Maurice Koch advanced funds to Apex Films, when in fact the funds were advanced by the partnership as well as by and through Producers Finance Corporation which was organized solely by the partnership for that purpose (R. 173-4).

This Court likewise erroneously concluded that a directed verdict was granted as against Maurice Koch when, in fact, the Court merely eliminated his claim based upon the loss of \$15,000 more than the amounts lost by the other partners, which ruling is contrary to the issues framed by the pleadings which admit the loss of the entire sum of \$90,000, including

the additional \$15,000 loss sustained by Maurice Koch. Just how the trial Court arrived at a finding that only \$75,000 was lost despite the plain facts, the issues as framed by the pleadings, and the realities of the situation will continue to remain a mystery which we fervently hoped would be resolved by this Court. The trial Court refused to hear from appellants upon the subject.

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**THE RULE ANNOUNCED BY THIS HONORABLE COURT REGARDING CONSIDERATIONS TO BE GIVEN TO ACTIVITIES OF THE TAXPAYER IN DETERMINING WHETHER OR NOT ONE IS ENGAGED IN A PARTICULAR BUSINESS IS IN CONFLICT WITH THE PREVAILING LAW PROMULGATED AND APPROVED BY THE SUPREME COURT AND ALL OF THE CIRCUITS.**

Note: We have mentioned that appellants were not in the business of making "loans", and that this Honorable Court is in error in stating that appellants made only one isolated "loan at the outside," when in fact appellants were constantly engaged during the entire year 1947 in "packaging" films and expended time, energy and funds consistently during said year for that purpose. We also note that this procedure continued prior to, as well as following the year in question.

In view of the peculiar facts of the case and the arguments and contentions made at the time of trial, appellants requested several instructions to the effect that time and effort expended for the purpose of advancing appellant's projects should be considered by

the triers of fact, and should be considered whether or not the same resulted in completed productions.

An appeal was taken to this Court upon the failure of the trial Court to instruct upon the subject as requested (see App. Op. Br. pp. 10 and 11; R. 23 to 26) and for the purpose of having the rule clearly enunciated that all activities of the taxpayer, including all time, all efforts and all funds expended in advancing the taxpayers' projects should be considered in determining whether or not the taxpayer is engaged in a particular trade or business.

This Court has announced its views upon that subject; however, these views are in conflict with prevailing authority. Prevailing authority upon the subject (see footnote 5, p. 40, appellants' opening brief) has established that all activities must be reviewed and considered. The decision of this Court on p. 5 states:

"Where appellant had made only one isolated loan at the outside, we do not think the jury could conclude that a number of futile transactions and activities looking toward consummation of loans had any value in determining whether the partnership was engaged in the business of financing."

Thus this Court has held that activities which do not result in concluded transactions have no value in determining whether a taxpayer is engaged in a particular business.

The decision of this Honorable Court holds that only activities relating to completed transactions may be considered in this vital determination.



We find no authority for the proposition that only concluded transactions, or that only fully produced film productions, or that only efforts expended upon concluded transactions may be considered in determining whether or not one is engaged in a business. No consideration is afforded the taxpayer who has devoted his time, effort, energy and substance when only one, or a very few, transactions are successfully culminated.

We note that that there are many large enterprises such as the independent film business, where numerous efforts result in but very few concluded transactions. Certainly, only concluded transactions are not fully probative of the time, effort, energy and substance expended.

---

**WHEN PERSONS FORMALLY AGREE TO ENGAGE IN A PARTICULAR BUSINESS AND ACCORDINGLY PROCEED TO ACT UNDER THE AGREEMENT, FURTHER INQUIRY IS IMPROPER.**

We note that here the taxpayers solemnly agreed by formal agreement to engage in the business of financing motion picture ventures some three years prior to the period in question; that they acted thereunder prior to the time in question, during the time in question, and after the time in question. There was no suggestion of fraud, and the Court actually found that their agreement was at all times in full force and effect.

In the absence of specific agreements the Courts have resorted to a consideration of the activity of the

persons involved in order to determine the amount of time, efforts, energy and funds expended for the purpose of establishing the fact in question by overt acts. When parties have stipulated their intentions in formal writing and have agreed and acted accordingly, it would appear erroneous to permit inquiry having far less probative value and not necessarily related to the particular act or transaction in question. Thus, if persons agreed formally to engage in the building business and actually built a building, why should Courts look further to establish the clear intent and purpose of the parties? We suggest that any rule which contravenes the formally expressed purpose, intent and act of the parties and permits inquiry into secondary evidence and *res inter alios acta*, should not be acceptable to this Honorable Court.

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**THIS COURT HAS ERRONEOUSLY HELD THAT THE BUSINESS OF FINANCING IS NOT A TRADE OR BUSINESS.**

Cases have been decided upon the peculiar facts of each case; however, there is no authority for the rule now announced by this Court that the business of financing, under a "common sense view", is not a trade or business.

This Court has stated:

"It may be that the jury took a common sense view and refused to recognize investment, management and other forms of financing as a trade or business."

The view, thus expressed, is inherently incorrect in fact as well as in law. It seems well settled that any

activity may be or become a business if conducted as a business. Financing is certainly no exception and has been a well-recognized basic business since the beginning of known civilization.

The pronouncement by this Court of a rule that financing, under a "common sense view", may not be regarded as a trade or business will create unexpected confusion in the law.

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**ERRONEOUS RULINGS RE REJECTION OF EVIDENCE HAVE NOT BEEN CONSIDERED BY THIS HONORABLE COURT, AND RULINGS CONSIDERED HAVE BEEN DETERMINED IN ERROR, BOTH IN LAW AND IN FACT.**

The most cogent inquiry involved the amount of time spent in connection with motion picture activities. The trial Court excluded testimony offered to prove the amount of time spent during the year in question (R. 2, R. 60; R. 245-246).

Numerous documents were presented and refused upon the ground that the same were not executed. Those that were executed, and due execution proved, were excluded on the ground that the name of appellants did not appear therein (R. 46, 210-212, 213-214, 78-85, 84-85, 99-100, 78, 88-89, 109, 124, 128-130, 92-93).

The opinion of this Court states:

"... the documents did not prove anything with regard to appellants. They were properly excluded."

These documents tended to prove the time, efforts, energies and funds expended in negotiation and in

packaging motion picture financing transactions. They are the various documents which tangibly demonstrate the various packaging efforts for each of the artistic elements, facilities, distribution of films, and financing. These are the ingredients which must be obtained, all at the same time, in order to make a film, and the record clearly demonstrated that it would be senseless to execute one agreement, for only one of the elements, unless all were available at the same time. The problem is inherent in the nature of independent film production.

The documents were not offered to prove the truth of their content. They were offered to show the time and effort expended, and further to show the intention of the partnership as indicated by the overt acts of negotiation which resulted in the documentation. The Court and jury could have reasonably drawn from these documents inferences supporting plaintiffs' position that time and negotiations continued and that funds were expended in such negotiations as well as in the drafting of the documents.

It was clear that the documents were offered for the purpose of proving activity, and not to prove that particular transactions were concluded. Of course, if the rule now announced by this Court in its present opinion should stand, efforts, negotiations, expenditures of time and all of their substance expended by these partners become meaningless; however, we fervently hope that this Honorable Court will reappraise its opinion in this regard.

## CONCLUSION.

We respectfully submit:

(1) that all causes, including the instant one, should be tried upon the basis of appropriate legal criteria;

(2) that the opinion filed by this Court will create confusion with regard to generally accepted principles prevailing in tax trials; and

(3) that the matter must be reconsidered and the opinion and decision of this Court revised.

We respectfully request that in the event appellants' petition for rehearing is denied, this Honorable Court permit hearing of this cause en banc in order that appropriate criteria respecting the trial of tax causes may be fully considered by this Court, and in order that appropriate instructions and rules of evidence may be applied for the benefit of litigants in such causes.

Dated, San Francisco, California,  
October 10, 1958.

Respectfully submitted,

MAX FINK,

LEON SCHILLER,

*Attorneys for Appellants  
and Petitioners.*

## CERTIFICATE OF COUNSEL.

Counsel in this cause certify that in their judgment the grounds stated in this petition for rehearing are well founded, and this petition for rehearing is not interposed for delay.

Dated, San Francisco, California,

October 10, 1958.

MAX FINK,

LEON SCHILLER,

*Attorneys for Appellants  
and Petitioners.*

**No. 15,645**  
**United States Court of Appeals**  
**For the Ninth Circuit**

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HAROLD M. KOCH, BESSIE KOCH, WIL-  
LIAM L. KOCH, ROSE KOCH, REBECCA  
KOCH ABEL, MAURICE P. KOCH, and  
DAISY KOCH,

*Appellants,*

VS.

UNITED STATES OF AMERICA,

*Appellee.*

**Appeal from the United States District Court for the  
Northern District of California,  
Southern Division.**

**APPELLANTS' OPENING BRIEF.**

---

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**FILED**

FEB 13 1958

PAUL P. O'BRIEN, CLERK





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# United States Court of Appeals For the Ninth Circuit

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HAROLD M. KOCH, BESSIE KOCH, WIL-  
LIAM L. KOCH, ROSE KOCH, REBECCA  
KOCH ABEL, MAURICE P. KOCH, and  
DAISY KOCH,

*Appellants,*

VS.

UNITED STATES OF AMERICA,

*Appellee.*

Appeal from the United States District Court for the  
Northern District of California,  
Southern Division.

## APPELLANTS' OPENING BRIEF.

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### I. JURISDICTION.

This appeal is from a judgment in favor of the United States of America rendered in the United States District Court for the Northern District of California, Southern Division, in an action brought by appellants pursuant to provisions of U.S.C. Title 28, Section 1346(a)(1), for the refund of income taxes alleged to have been erroneously paid, collected and retained by appellee (R. 13-15).

The complaint alleged jurisdiction pursuant to U.S.C. Title 28, Sec. 1346(a)(1) (Supp. R. 383, Paragraph I).

Appellants Harold M. Koch, William L. Koch, Maurice P. Koch and Rebecca Koch Abel are partners in the firm of Koch & Sons, and appellants Bessie Koch, Rose Koch and Daisy Koch are respectively the spouses of the three appellants first named. Each appellant filed separate income tax returns for the years in issue.

Judgment was entered on January 23, 1957 (R. 13-15). A motion for new trial was filed February 1, 1957 (R. 21, 22), and an order denying said motion was made March 5, 1957 (R. 22). Notice of appeal to this Honorable Court was filed with the District Court on April 18, 1957 (R. 32) pursuant to the provisions of Sections 1291 and 1294(1) of 28 U.S.C. and within the time provided by Rule 73(a) of Federal Rules of Civil Procedure, 28 U.S.C.

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## II. STATUTES INVOLVED.

The pertinent portions of the Revenue Code involved, and in effect at the time in question, are as follows:

1939 I.R.C. Section 23.

“Deductions from Gross Income.

“In computing net income there shall be allowed as deductions: . . .

“(e) Losses by Individuals. In the case of an individual, losses sustained during the taxable year and not compensated for by insurance or otherwise—

“(1) if incurred in trade or business;

“(k) Bad Debts.

“(1) General rule. Debts which become worthless within the taxable year; . . . This paragraph shall not apply in the case of a taxpayer, other than a corporation, with respect to a non-business debt, as defined in paragraph (4) of this subsection.

“(4) Non-business debts. In the case of a taxpayer, other than a corporation, if a non-business debt becomes worthless within the taxable year, the loss resulting therefrom shall be considered a loss from the sale or exchange, during the taxable year, of a capital asset held for not more than 6 months. The term ‘non-business debt’ means a debt other than a debt evidenced by a security as defined in paragraph (3) and other than a debt the loss from the worthlessness of which is incurred in the taxpayer’s trade or business.

“(s) Net Operating Loss Deduction. For any taxable year beginning after December 31, 1939, the net operating loss deduction computed under section 122.”

The pertinent portions of I.R.C. 122 relating to carry-back to previous taxable years of losses subsequently incurred are as follows:

“Sec. 122. Net Operating Loss Deduction.

“(a) Definition of Net Operating Loss. As used in this section, the term ‘net operating loss’

means the excess of the deductions allowed by this chapter over the gross income, with the exceptions, additions, and limitations provided in subsection (d).

“(b) Amount of Carry-Back and Carry-Over.

“(1) Net operating loss carry-back.

“(A) Loss for taxable year beginning before 1950. If for any taxable year beginning after December 31, 1941, and before January 1, 1950, the taxpayer has a net operating loss, such net operating loss shall be a net operating loss carry-back for each of the two preceding taxable years. . . .

“(d) Exceptions, Additions, and Limitations. The exceptions, additions, and limitations referred to in subsections (a), (b), and (c) shall be as follows:

“(5) Deductions otherwise allowed by law not attributable to the operation of a trade or business regularly carried on by the taxpayer shall (in the case of a taxpayer other than a corporation) be allowed only to the extent of the amount of the gross income not derived from such trade or business.”

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### III. STATEMENT OF CASE.

This action involves a determination as to whether or not the losses incurred by taxpayers in the year 1947 were deductible as losses incurred in the taxpayers' trade or business as provided in 1939 I.R.C. Sec. 23(e)(1) or Sec. 23(k)(1), and in the operation



of their business within the meaning of the "carry-back" provisions of 1939 I.R.C. Sec. 122.

### **1. The Pleadings.**

The complaint alleged, in separate counts for each of the partners and their respective spouses, a loss in the year 1947 attributable to a business carried on in that year. (S.R. 389, paragraph VI; S.R. 393, paragraph VI; S.R. 397, paragraph VI; S.R. 401, paragraph VI; S.R. 404, paragraph VI; S.R. 409, paragraph VII; S.R. 413-414, paragraph VII).

The answer admits that the total sum of \$90,000.00 was expended and resulted in loss in the year 1947; however, the answer alleges that the loss was a non-business bad debt and therefore requires tax treatment as a capital loss. (S.R. 417, paragraph 6; S.R. 418, paragraph 12; S.R. 426, paragraphs 2 and 5).

### **2. The Trial.**

All motions, issues and facts were determined by the Court, except that by stipulation (R. 293), a single special interrogatory was submitted to the jury, to-wit:

"During the year 1947, was H. Koch & Sons regularly engaged in the business of financing motion picture ventures?"

### **3. Fact Pattern.**

Three brothers and a sister, members of the Koch family, entered into a partnership agreement on December 31, 1941 (Appendix A, Exhibit 1, R. 35), under the firm name of H. Koch & Sons. Although

the partnership originally conducted a luggage business previously conducted by the father of the partners, the agreement was amended on October 23, 1944 to provide that the partnership would engage *in the business of financing motion pictures* (R. 35, 36, Exhibit 2; portions reprinted in Appendix B).

#### 4. Theories Upon Which the Cause Was Presented.

A. Plaintiffs' theory upon trial of the cause was two-fold: Firstly, that they acted pursuant to their formal partnership agreement (Appendix B) to engage *in the business of financing motion picture ventures*, and that they were so engaged when the loss occurred and are therefore entitled to the deductions provided by 1939 I.R.C. Sections 23(e)(1) or 23(k)(1) and Section 122 as a matter of law; and

Secondly, that the motion picture financing transaction which resulted in loss was not an isolated transaction, and plaintiffs offered proof of extensive activities in similar motion picture financing transactions during the period in question, and urged that time and effort expended in said business should be considered with respect to all transactions and whether or not the same resulted in concluded financing agreements.

B. The Government's theory of the case, in which it was largely supported by the trial Court, was: That only actual investments which were concluded during the exact period in question should be considered in determining whether or not the partnership was engaged in such business, and that the extensive nego-

tiations and time and effort spent in the business which did not result in actual concluded financing within the exact limits of the year in question, were to be disregarded.

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#### IV. QUESTIONS PRESENTED.

1. Charge to the jury: Did the trial Court err in giving instructions contrary to the law, in its failure to give properly requested instructions necessary to a determination of the cause, and in failing to give any properly requested instruction upon plaintiffs' theory of the case?

2. Directed verdict: Was the trial Court in error in granting a dismissal or directed verdict (as the case may be) with regard to part of the relief sought, and particularly when the erroneous ruling affected all other considerations in the cause?

3. Evidence: Was the trial Court in error in its rulings with regard to the admission and rejection of evidence?

4. Findings: Are the findings supported by the pleadings, the evidence, and the stipulations of the parties?

5. Conclusions: Did the trial Court erroneously determine the law applicable to the particular facts and issues presented?

6. Sufficiency of evidence: Is the judgment supported by the evidence?

7. Argument of counsel: Were plaintiffs prejudiced by the misconduct of counsel which misled and inflamed the jury and by reason of which plaintiffs were prevented from having a proper deliberation by the jury?

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## V. SPECIFICATIONS OF ERRORS.

### A. ERRORS IN THE CHARGE OF THE COURT TO THE JURY.

(1) The trial Court instructed:

“If you believe that Maurice P. Koch used his own money in any transaction and was acting therein in his own behalf and not on behalf of H. Koch & Sons, that transaction cannot be considered by you in determining whether the partnership of H. Koch & Sons was engaged in the business of financing motion picture ventures.”  
(R. 302.)

Exception was taken (R. 311, 312). The trial Court had granted a directed verdict (or dismissal) against Maurice P. Koch upon the basis that there was no evidence that he had ever acted in his own behalf, and that all of the evidence and the agreement of the parties conclusively established that all of his acts were on behalf of the partnership (R. 292). After Maurice P. Koch was thus put out of the case, the Government argued the “Janus-faced” plea to the jury that the activities were all the personal activities of Maurice P. Koch in his own behalf and not in behalf of the partnership (R. 353, 354). There was

no theory of fact in the case as a basis for the instruction. The instruction compounded the error of the Court and the prejudicial remarks of counsel.

(2) After extensive evidence was received upon the issues the Court instructed the jury:

“There is a presumption that the determination by the Commissioner of Internal Revenue that the plaintiffs were not engaged in the trade or business of financing motion pictures is correct. The burden is upon the plaintiff to overcome the presumption of the correctness of the Commissioner’s determination by proving by a preponderance of the evidence that they were engaged in the trade or business of financing motion pictures.” (R. 301-302.)

This instruction was further impressed by the Court’s statement to the jury as follows:

“Thereafter the Commissioner of Internal Revenue *made a determination* that the loss incurred by H. Koch and Sons was not as the result of a business bad debt but that the loss occurred by reason of a nonbusiness bad debt.” (R. 298.)

We acknowledge, with apology, that the record does not contain the argument and authorities submitted upon this subject, except that during defense counsel’s argument to the jury (R. 343, 344), and before the Court instructed the jury, plaintiffs objected to the proposition propounded by the instruction, and the ends of justice require consideration of the fatal error involved. Under the decisions of this Honorable

Court, the Commissioner's determination merely shifts the burden of going forward, and once there is evidence, the cause must be decided "upon the evidence and upon the evidence alone." (Note: The trial Court's own findings are based on the alleged "presumption.")

(3) The trial Court failed to give to the jury any one of the instructions properly requested by the plaintiffs upon plaintiffs' theory of the case as follows:

"That in determining whether or not H. Koch & Sons was engaged in the business of financing motion picture ventures, you must consider, among other things, the amount of time and effort expended in that direction, and such time and effort, if any, must be considered by you whether or not an actual venture was concluded."

"That in considering the activities of H. Koch & Sons with relation to the business of financing motion picture ventures, you must consider all activities designed to advance the financing of such projects and you must consider the same whether or not the transactions were actually concluded."

"That in considering the question as to whether or not H. Koch & Sons devoted substantial time to the financing of motion picture ventures you are required to consider all of their activities relating to that purpose, and all activities and efforts actually expended in attempting to negotiate for and in attempting to enter into financial transactions relating to the business of financing motion picture ventures must be considered by you upon this issue, whether the same were concluded or not." (R. 25 and 26.)

Exceptions were taken for the failure to give any one of these instructions (R. 31). The jury was left with the impression that "financing" means paying out money and that all time, efforts and transactions in which actual funds were not disbursed were to be disregarded. The requested instructions express the law and plaintiffs' entire theory of the case.

(4) The trial Court failed to give any one of the instructions properly requested by plaintiffs as follows:

"In order for one to be regularly engaged in the conduct of a particular business, it is not necessary that he devote a major part or any particular part of his time and efforts to such business. Neither is it necessary that he devote a major portion or a particular portion of his capital to such business in order for it to be deemed to be a business regularly carried on by such taxpayer. . . . etc." (R. 23-24.)

"A taxpayer may be deemed to be regularly engaged in the conduct of a particular business even though he may devote most of his time, efforts, and capital to another business or other businesses." (R. 24.)

"That if you should find that H. Koch & Sons, acting through one or more of its partners, or acting through persons, firms, corporations or representatives appointed by said partnership, has regularly and continuously participated in the promotion and financing of motion picture ventures during the year 1947, then you must find that H. Koch & Sons was engaged in the business of financing and promoting motion pic-

ture ventures and that said business was regularly conducted." (R. 25.)

In the absence of these instructions, as well as any instruction relating to plaintiffs' theory of the law of the case, the jury remained uninformed with regard to any basis upon which it could predicate an answer in favor of plaintiffs.

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#### **B. ERRORS OF LAW.**

(1) The Court erred as a matter of law in its interpretation of the copartnership contract of the parties (Exhibit 2, Appendix B), and further erred by reason thereof in granting a directed verdict (or partial dismissal) with regard to the claims of Maurice P. Koch and his wife, Daisy Koch.

(2) The trial Court erred in granting a directed verdict (or partial dismissal) with respect to the plaintiffs Maurice P. Koch and Daisy Koch.

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#### **C. ERRORS WITH RESPECT TO THE ADMISSION AND REJECTION OF EVIDENCE.**

(1) The Court erred in its failure to admit into evidence Exhibit 5 for identification (Appendix D) (the contract between one Coslow and United Artists Corporation for the production and world-wide distribution of a feature film, and providing that Coslow must be the controlling stockholder of the corporation producing same). The loss in question (\$90,000.00)



occurred in activating said corporation and in the advancements made for the pre-production costs of the film contemplated by the agreement. The document was finally excluded upon the ground that it had no bearing on the issues of the case.

This document was offered and rejected several times. It was first objected to on the ground that no foundation was laid (R. 46). The foundation was laid (R. 210-212), whereupon the Court refused to admit the document (R. 212). Document offered again and the Court could not find the name of the plaintiffs in the document and refused to permit counsel to explain the interest and beneficiary position of plaintiffs in this agreement (R. 213-214).

(2) The Court erred in its failure to admit into evidence Exhibit 19 for identification (Appendix E) (an unsigned document negotiated to set up a venture for the financing and production of a series of films between plaintiffs and several well known creative persons in the film industry).

The document was offered for the purpose of showing the activities of the plaintiffs in the business of financing motion picture ventures, to show the time and effort expended in negotiations, and as a physical fact indicating efforts expended at the very time in question (R. 79-81), and as a key to the time, effort and expenses incurred. The offer was renewed (R. 84-85) and the purpose clearly demonstrated.

Objection was made on the ground that the document was prepared in the name of the partnership's

wholly owned corporation, Ambassador Productions, and not in the name of the partnership (R. 85). The Court refused admission on its own objection that the document was not executed, i.e., that the actual advancement of funds was not consummated (R. 85).

(3) The Court erred in its failure to admit into evidence Exhibit 21 for identification (Appendix F) (an unexecuted agreement between one of the partnership's wholly owned corporations and Alfred E. Green, dated April 28, 1947, providing for the employment by said corporation of Alfred E. Green in the capacity of director and producer for a series of films over a period of three years). This was also offered to show time expended, and refused because not executed. Objection was made on the ground that the agreement was not with plaintiffs but with their wholly owned corporation. The Court sustained the objection only upon its own objection that the document was not executed (R. 84-85).

(4) The Court erred in its failure to admit into evidence Exhibit 26 for identification (Appendix G), which is the unexecuted contract negotiated in the period in question between Monogram Pictures Corporation and Ambassador Productions, Inc. (plaintiffs' wholly owned corporation) for the financing, production and distribution of a series of films, together with a letter dated September 25, 1947, from Monogram Pictures Corporation to the attorneys for the partnership.

The document was evidence of the time, effort and expenditures incurred in negotiations for a series of

films at the exact time in question. Objection was made that no foundation was laid; and the Court refused admission on the ground that the document was not executed (R. 99-100). Stipulation covered foundation in so far as preparation and receipt of documentation was concerned (R. 99); however, the Court excluded the same upon the ground that the agreement was not executed and concluded (R. 100).

(5) The Court erred in its failure to admit into evidence Exhibit 29 for identification (Appendix H). This exhibit was offered to prove that negotiations for the financing of a series of films to be produced by Monogram Pictures, commenced in September, 1947, were still under way on November 19, 1947 (the period in question). Objection was raised on the ground that the letter from Monogram Pictures was addressed to the attorney for the partnership, who also formed and happened to be a director, with his co-counsel, of the partnership's wholly owned corporation, Ambassador Productions, and upon the ground that there was no showing which of the capacities of the attorney applied in the receipt of this letter (R. 107-108). The Court sustained the objection upon this ground, although the record is completely clear that counsel were acting for the partnership at all times (R. 78, 88-89, 109, 124).

(6) The Court erred in its failure to admit into evidence the check payable to Apex Film Corporation, dated January 26, 1948, and evidence of the details of advances made thereafter. Although the loss in

question occurred in the year 1947 and the transaction for the financing of this large series of films was conducted in 1947 the funds were not advanced until January, 1948. The Court refused to admit the detail evidence of actual funds advanced in 1948 pursuant to arrangements made in 1947 (R. 128-130) although the Court previously ruled, in effect, that only concluded transactions and funds actually advanced were to be considered, and likewise had ruled that only the details of transactions would be admitted (R. 60, 245-246).

(7) The Court erred in refusing Exhibit 24 for identification (Appendix I) (a letter from Annie Laurie Williams, dated October 17, 1946, opening the negotiations for "Hill of the Hawk" by Scott O'Dell).

The letter was admittedly received by counsel for plaintiffs in motion picture transactions (R 92). The Court refused to admit this correspondence showing the commencement of this project which continued as a major activity throughout the entire period, on the grounds of "hearsay" (R. 92-95). The letter was not offered to prove the truth of its contents. It was offered to prove activity.

(8) The Court erred in sustaining objection to testimony offered to show the quantum of time and effort expended in picture transactions.

The Court refused to permit testimony with regard to the number of transactions and the amount of time and effort expended on the grounds of "vague, speculative, and calling for the opinion and conclusion

of the witness". Mr. Koch was asked how many different deals were looked into over a six month period. Defense objected on the grounds, vague and speculative, calling for the opinion and conclusion of the witness. The Court stated,

"I think in view of the objection he would have to give the individual contacts" (R. 60).

(9) During the course of taking testimony of a disinterested witness who had been present at almost all negotiations, the Court similarly erred in sustaining objection as follows (R. 245-246):

"Q. (By Mr. Fink.) So far as *your own personal knowledge is concerned*, with regard to the year 1947, approximately what part of Mr. Koch's time did he spend in connection with motion picture activities?

Mr. Gillard. I object to that as calling for the opinion and conclusion of the witness.

The Court. Sustained." (Emphasis ours.)

(10) Although defendants made proof that plaintiffs sold out certain assets some years later, the Court refused to permit testimony to prove that plaintiffs went out of the motion picture financing business only after some years following the time in question (R. 181-182), on the erroneous ground that the question making inquiry as to when they went out of this business called for the conclusion of the witness.

**D. SPECIFICATION OF ERRONEOUS FINDINGS.**

(1) Finding No. 5 (R. 8) that H. Koch & Sons were in the luggage business is erroneous, confusing and misleading in light of consideration of Finding No. 2 (R. 8). Finding No. 2 determines that the formal agreement of the parties executed in 1944, was in full force and effect at all times and provided that the partnership would engage in the business of financing motion picture productions; whereas Finding No. 5 determines that the partnership was *only* in a different business contrary to the contract and acts of the partners.

(2) The complaint alleges and the answer admits losses in the total sum of \$90,000 and not \$75,000 as found in Finding No. 6 (R. 8-9). (S.R. 385, paragraph VI; S.R. 405, paragraph II; S.R. 417, paragraph 6; S.R. 426, paragraph 2). The finding is likewise erroneous in that the said finding and the findings as a whole do not dispose of the loss sustained by Maurice P. Koch (and his wife, Daisy) of amounts contributed pursuant to the partnership agreement in excess of the participation by the other partners. This finding also fails to show that the partnership was in fact the largest owner of interest in the film. The finding is not supported by the evidence.

(3) Finding No. 8 (R. 9) assumes that the plaintiffs are bound by the findings of the Collector of Internal Revenue. Such a presumption or inference is a mere rule of evidence or of "going forward" and disappears upon the introduction of evidence. Here

we have the glaring error of the trial Court in making a finding based upon an alleged presumption; whereas this Honorable Court has repeatedly held that the "presumption" disappears upon the introduction of evidence, and that when evidence has been introduced, determinations must be made upon the evidence and upon the evidence alone.

(4) The Court erred in Finding No. 9 (R. 10) that the loss resulted from a non-business bad debt. This finding is not supported by the evidence. The finding is erroneous in that the ultimate fact to be found by the Court is whether or not the loss incurred was *attributable to the operation of a trade or business conducted by the plaintiffs* (1939 I.R.C. Sec. 23 (e)(1), Sec. 23(k)(1), Sec. 122(d)(5)).

(5) The Court erred in its Finding No. 10 (R. 10) to the effect that Maurice P. Koch was not engaged in the business of financing motion picture ventures. He was thus engaged pursuant to the express terms of the partnership agreement and all his acts were conducted as manager of the partnership business.

(6) Findings Nos. 11 and 12 (R. 10) find that by stipulation of the parties all of the salient and ultimate issues were withdrawn prior to submission of the case to the jury. No such stipulation was made and no issues were withdrawn. Only one special interrogatory was agreed upon and the parties carefully preserved by stipulation that all other facts and issues would be passed upon by the Court (R. 293). These findings also incorrectly interpret the allegations of the complaint.

The ultimate issue of fact in the entire cause is the determination as to whether or not the loss incurred was attributable to the operation of a trade or business. Findings 11 and 12 are only an attempt to hurdle the requirement of a finding on this, the ultimate issue of fact in the case, by substituting or adding stipulations which were not made, and by erroneous interpretation of the complaint.

(7) Finding No. 12 (R. 10, 11). The Court finds that a stipulation was made that limited plaintiffs' basis of recovery. No such stipulation was made and the record demonstrates the contrary (R. 293). The only interrogatory upon which the parties could agree was as quoted; however, the stipulation clearly preserved the duty of the Court to pass upon all other questions of fact, as well as law, and the duty of the Court to resolve all of the ultimate issues in the case.

(8) The Findings as a whole are erroneous in that they fail to find upon the ultimate fact in the case, to wit: Was the loss incurred "attributable to the operation of a trade or business?"

(9) The Findings as a whole are in error because they are based upon alleged stipulations which were not in fact made.

(10) The Court erred in its failure to make a finding as proposed by plaintiffs' number 4 (R. 17):

"The said Maurice P. Koch was entitled to share proportionately to the extent of the sum of \$75,000 contributed by the partnership and entitled to a separate share for the additional funds advanced by him and which were not matched by the remaining partners."



**E. ERRONEOUS CONCLUSIONS OF LAW.**

(1) Conclusion No. 1 (R. 11) is in error in that the Court concluded that the loss was not incurred in the trade or business of H. Koch & Sons. Proper interpretation of the agreement and acts of the parties (Ex. 2, Appendix B) requires the conclusion that the loss was incurred in the trade or business of H. Koch & Sons. The conclusion is erroneously based upon the Court's finding in accordance with an alleged "presumption" that the Commissioner of Internal Revenue had made a correct determination.

(2) Conclusions of law Nos. 2, 3, 4, 5, 6 and 7 and each of them (R. 9-10) are in error for reasons as follows: (i) The same are based upon findings which are not supported by the evidence; (ii) The same are based upon stipulations which are non-existent and which are contrary to all intendments of the record; (iii) The same are erroneous because they are contrary to an appropriate legal interpretation of the written agreement of the parties; (iv) The same are contrary to the content, allegations, admissions and issues as framed by the pleadings; (v) They are based upon an alleged presumption favoring the Commissioner which erroneously survived all evidence in the cause; (vi) The Conclusions as a whole fail to conclude the law upon the ultimate legal issue in the case, to wit, Was the loss involved attributable to the operation of a trade or business?

**F. THE JUDGMENT IS NOT SUPPORTED BY THE EVIDENCE.**

The evidence is susceptible to only one reasonable interpretation, to-wit, that appellants' loss was incurred in the course of activities attributable to the operation of their business. The judgment is based upon stipulations, assumed and which do not exist, upon improper findings and erroneous conclusions. The judgment is based entirely upon an erroneous concept of the effect of the alleged "presumption" of correctness of determinations by the Commissioner of Internal Revenue. Once the several decisions and rules of this honorable Court are applied, the alleged presumption must fall, leaving all of the evidence overwhelmingly favoring plaintiffs.

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**G. PLAINTIFFS' CAUSE WAS PREJUDICED BY MISLEADING AND INFLAMMATORY STATEMENTS MADE BY COUNSEL FOR THE RESPONDENT.**

The prejudicial and inflammatory statements by counsel for defendant caused a miscarriage of justice. Statements that this was plaintiffs' second crack at the case because plaintiffs had already lost the case once before the Commissioner; that plaintiffs' counsel were merely laying down a smoke screen, etc., and these statements being made by a representative of the people could hardly make for justice.

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**VI. ARGUMENT.****A. THE FACTS.**

Appellants, Maurice P. Koch, Harold M. Koch and William L. Koch, were brothers, and appellant

Rebecca Koch Abel is their sister. The remaining appellants are the respective wives of the brothers. On December 31, 1941, the brothers and sister formed a partnership (R. 35, Ex. 1, Appendix A), under the style of H. Koch & Sons. The partnership became the successor to a luggage manufacturing business previously conducted by the father of the partners (R. 45). The brothers Harold and William were shop workmen, Rebecca kept the books, and Maurice (also referred to as Murray) (R. 266) was the general manager and so-called "boss" or "outside man" (R. 266). He received special compensation and privileges (Ex. 1, Appendix A) and was completely in charge (R. 44, 45) to the extent that partnership dealings and written documents were quite often in his own name (R. 72, 76). Pursuant to agreement (Ex. 2, Appendix B) all documentation in the picture business was drafted in the name of Maurice P. Koch and the partnership style is not mentioned (Plaintiffs' Ex. Nos. 10, 12, 14, 16, 17 in evidence, Appendix K, L, M, N and O, respectively). The funds, which were admittedly lost, were disbursed from the partnership upon checks generally signed by Rebecca, and at times by Maurice (Plaintiffs' Ex. Nos. 6, 8, 10A and 13 in evidence, Appendix P, Q, R and J, respectively). It was clearly established that all references to Maurice P. Koch refer to the partnership (R. 43, 101); that whenever Maurice refers to "my people" he is referring to his partners (R. 56, 57); that he executed the documentation on behalf of the partnership, although the same was in his own

name (R. 72); that although he was expressly authorized in writing to conduct the transactions in his own name, there was also a practice to use his name instead of the name of the partnership (R. 76); that when he organized corporations to further the motion picture investment projects, he was at all times acting and signing on behalf of the partnership although his own name appeared (R. 96, 97). During all of the times mentioned, and throughout all motion picture transactions, Maurice acted for, and only on behalf of, H. Koch & Sons, a copartnership (R. 112); although stock of corporations engaged in motion picture activities stood entirely in his name, the stockholder was in reality the partnership (R. 122, 123, 124); in addressing Maurice in the record or otherwise, the use of the word "you" indicated H. Koch & Sons (R. 101, 125); and the attorneys engaged for picture purposes in fact represented H. Koch & Sons (R. 78, 88-89, 109, 124, 191).

Maurice P. Koch's lifetime associations, friendships and relationships were in the motion picture business (R. 37). In 1944 the activities of H. Koch & Sons were quite limited, and generally related to the luggage business (R. 267). Competition was extremely keen and the future appeared bleak for that industry (R. 181).

The decision of the partnership to engage in the business of financing motion pictures is fully confirmed by two formal documents both bearing date of October 23, 1944, some three years prior to the particular loss in question, as follows:

(1) The written amendment to the partnership agreement (Ex. 2, Appendix B), which provides that the partnership will engage in the business of financing motion picture ventures by each and every means, and that all partnership resources be available to this purpose.

(2) On the same date upon which this partnership agreement was entered into, the partners formed "Producers Syndicate" (R. 36, 37, Ex. No. 3, pertinent portions reprinted in Appendix C).

*The trial Court found (Finding No. 2, R. 8) that the partnership agreement providing that the partnership was engaged in the business of financing motion pictures, was in full force and effect at all times. After executing this partnership agreement, all of the activities of Maurice P. Koch in connection with the motion picture field were conducted pursuant to the authority contained in the agreement (R. 139, 140). His time, effort and expenses in motion picture matters were all paid for by the partnership (R. 112, Ex. 2, Appendix B). H. Koch & Sons were primarily interested in the "pre-production" phases of motion picture financing;<sup>1</sup> that is, in supplying the funds*

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<sup>1</sup>Pre-production financing presents the greatest risk and therefore also offers the highest rate of return. The partners all agreed to this type of pre-production financing (R. 42). Pre-production money is also sometimes referred to as "front money" (R. 226, 227) for the purpose of forming the company, acquiring rights to literary properties and artistic talents and facilities. All transactions were in the so-called independent field of the motion picture industry, and for the most part were in the "pre-production" phase (R. 40, 42, 196, 226, 227, 229, 230).

necessary to prepare and develop motion picture projects ("packaging"), as distinguished from actual film production.

It is expected that "front money" will be repaid when the picture is produced and the partnership intended to revolve its funds from picture to picture (R. 40, 42, 196, 226, 227, 229, 230). Partnership cash was limited (R. 180, 273); nevertheless, the partnership was using substantially all of its funds in this manner. The unfortunate and admitted loss created delays and difficulties in concluding financing arrangements on subsequent films in 1947, because these frozen and ultimately lost funds could not be revolved into additional planned projects.

The complaint alleges (S.R. 385, paragraph VI; S.R. 405, paragraph II) and the answer admits (S.R. 417, paragraph 6; S. R. 426, paragraph 2) that of the total funds utilized by the partnership in activating Beacon Pictures and its film "Copacabana", \$90,000 became a complete loss in the year 1947.

Appellants contend that their agreement to engage in the business of financing motion picture ventures, plus the fact that they acted thereunder, was adequate, as a matter of law, to establish that the loss which occurred was "attributable to the operation of their trade or business". The trial Court did not concur in this contention. Appellants thereupon offered extensive evidence of the activities of the partnership in motion picture financing, and demonstrated a constant, continuous course of such business, and exten-

sive and valuable time, efforts and funds expended (limited by the trial Court's rulings).<sup>2</sup>

The evidence established that in the year 1947, extensive, valuable and consistent time, funds and efforts were expended on the Beacon Pictures' "Copacabana" (R. 63, 67, 68, 75, 76, 77, 80, 132, 134, 159, 191, 192, 201, 202, 208, 209, 210, 213, 214, 215, 216, 218, 220, 221, 231, 247). That constant and repeated activities, time, efforts and funds were expended during the exact period in question with regard to many film projects is demonstrated by the record:

Ambassador Films (R. 81, 82, 83, 85, 86); The Alfred Green Negotiations (R. 77, 78, 83, 84, 87); The Jack Chertok Venture (R. 89, 90, 91, 195, 196, 238, 239, 240); The Producers Finance Venture (R. 95, 97, 165, 166, 183, 184, 192, 193, 194, 198); The Hill of the Hawk Venture (R. 91, 93, 94, 95, 108, 110, 113, 114, 122, 123, 124, 161, 176, 240, 241, 242, 243); Long November (R. 62); The Fred Fisher Story (R. 82, 104, 106, 234, 235); The Monogram Series (R. 98, 99, 100, 107, 111, 112, 236, 237); Thirty Government Training Films (R. 91, 92, 125, 126, 127, 128, 129, 130, 197, 198, 199, 244); Apex Films Corporation (R. 173, 174).

When we consider that each production is a major effort, requiring time to formulate, and when we consider the same in proportion to the resources of H. Koch & Sons, this was indeed an overwhelming show-

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<sup>2</sup>The rulings of the trial Court are noted in the exceptions to the rulings on the evidence, *supra*, and in the discussion of same, *infra*. Considerable and most cogent testimony and documentary evidence was excluded by the trial Court's rulings.

ing. We seriously doubt that any independent individuals, in the field of financing motion picture ventures throughout the world, did as much during the period in question. Appellants urge that these facts be considered in the light of the *written agreement of the partners to engage in the business of financing motion picture ventures.*

Although delayed and hampered by the unfortunate loss in 1947, the partnership continued to raise money by each and every means and use its resources for financing motion pictures. The record (citations above) discloses that as the year 1947 came to a close, the partnership was most active: The Monogram Series was pending; Ambassador Productions purchased "Hill of the Hawk" and was preparing it for filming, the Apex Films' arrangements for the production of more than thirty Government training films was underway; Producers Finance was owned and controlled by the partnership and was advancing funds; Ambassador Productions was wholly owned and controlled by the partnership; large bank borrowings were arranged; and activities were constant.

The income of the individual partners of H. Koch & Sons in the year 1947, and before deducting the \$90,000 loss incurred in the Beacon transaction, was in the sum of \$4,805 each, and the company had no funds (R. 180, 273). Under these circumstances, we particularly note the fund raising efforts and the very substantial funds which were expended and contributed in the course of motion picture financing ventures as disclosed by the entire record (R. 13, 53, 55,



58, 59, 66, 68, 69, 70, 73, 74, 91, 92, 116, 154, 163, 263, 264, 271, 116, 117, 118, 119, 122, 123, 124). The lack of funds and earnings from other sources, when compared with the amounts involved in motion picture activities, dramatically emphasizes the fact that motion picture activity was all important, and "related to the business" of the partnership and not an "isolated or casual" investment. Valuable time was expended not only by the partnership but also by their attorneys in San Francisco as well as in Los Angeles, and by representatives appointed by them (R. 43, 50, 78, 109, 127, 152, 189, 193, 200, 245, 257).

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#### **B. THE PARTNERSHIP AGREEMENT.**

The written partnership articles provided that the partnership would engage in the business of financing motion pictures (Ex. 2, Appendix B). The trial Court found that the agreement was in full force and effect at all times (Finding No. 2, R. 8). We note, particularly, that the partnership did not attempt at any time to receive "capital gain" treatment with regard to its operations relating to films. However, and for example only, if the partnership had profited in the year 1947 from the sale of an interest in a film, obviously it could not obtain "capital gain" treatment with regard to such sale. It would be foreclosed from "capital gain" treatment by the very terms of its partnership agreement providing that it was in this business. Certainly the taxing authorities would not permit "capital gain" treatment from a sale of an

interest in a motion picture venture to one who has an agreement with another *to engage in the business of financing motion picture ventures*. Having decided to be in such a business, its profits are classified as ordinary income as a matter of law. Therefore, it cannot be maintained that its losses are not likewise related to the operation of its business.

The agreement provides (Ex. 2, Appendix B): (1) That the partnership engage in the business of financing motion picture productions; (2) All assets (funds and credit) of the partnership were made available for this business; (3) Any money advanced by an individual partner over and above sums advanced by the partnership are first refunded to the partner making the advance, and such partner receives a proportionately large share of the profits and losses.<sup>3</sup>

4. Maurice P. Koch is to manage this part of the business in his own name or otherwise and all of his expenses incurred are paid by the partnership.

The loss was admitted. The complaint pleaded in its various counts loss of the total sum of \$90,000. The answer admitted the loss thereof in the year 1947.

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<sup>3</sup>This does not mean that by making an additional contribution or borrowing for the partnership the particular partner is acting outside the scope of the partnership activity. In this respect the trial Court was considerably confused and in error in its interpretation of the agreement and the pleadings. The complaint alleges that the sum of \$15,000 was advanced by Maurice P. Koch *in the same manner* as the funds which were advanced generally by the partnership (S.R. 405, Paragraph II). All of the funds lost were disbursed from partnership funds, by checks drawn upon the partnership, including the sum for which Maurice P. Koch is entitled to additional loss credit.

The Court found, contrary to the issues framed by the pleadings, that only \$75,000 was lost (Finding 6, R. 8-9).

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### C. INSTRUCTIONS.

1. The trial Court erred in giving instructions contrary to the law combined with prejudicial misconduct of counsel.

(a) In view of the failure on the part of the trial Court to give proper application to the partnership agreement which provided that the partners were in the business of financing motion picture ventures, evidence was introduced showing that the activities of the partnership were sufficient, even in the absence of such agreement, to remove the situation from an "isolated" transaction, into a loss "attributable to the operation of a trade or business". The activities, the number thereof, continuity, time, effort and intent, all became probative factors in the case.

The trial Court erroneously charged as follows:

"If you believe that Maurice P. Koch used his own money in any transaction and was acting therein in his own behalf, that transaction cannot be considered by you in determining whether the partnership of H. Koch & Sons was engaged in the business of financing motion picture ventures." (R. 302.)

The record was as follows:

(i) The evidence was clear and without contradiction that each and all of Maurice P. Koch's acts were for and on behalf of the partnership (see *supra*; also R. 43, 44, 45, 72, 76, 96, 97, 101).

(ii) The written terms of the agreement of the partners established as a matter of law that Maurice P. Koch could only act for the partnership. Not only did the amended partnership agreement (Ex. 2, Appendix B) so provide, but the original partnership agreement (Ex. 1, Appendix A) required that he devote his exclusive and full time and effort to partnership activities.

(iii) Maurice P. Koch borrowed \$15,000 and contributed same to partnership funds in order to make that amount available to the partnership to cover some of the motion picture expenditures previously made (R. 287). Therefore, Maurice P. Koch and his wife sought recovery for this additional \$15,000 loss suffered by them pursuant to the partnership agreement (Appendix B). However, the court misinterpreted the agreement, and erroneously held that in order to receive credit for the additional \$15,000 loss, Maurice P. Koch had to be individually engaged (as distinguished from the partnership) in the business of financing film ventures. Admittedly, he was not individually engaged in any business and that all of his activities were for the partnership. Therefore, the Court granted a directed verdict (or dismissal) as to Maurice P. Koch's claim for allowance of the additional \$15,000 loss suffered by him (and his wife), without hearing from appellants on this matter. (R. 292).

The pleadings admitted that the \$15,000 especially attributable to Maurice P. Koch as well as all other sums making up the \$90,000, were expended and lost.

The defense attempted to amend their pleadings (R. 290) and this motion was denied (R. 292) with the result that at the time the cause was submitted to the jury the loss of the entire \$90,000 was admitted by the pleadings. Although the Court was in error, this ruling of the Court, coming after plaintiffs rested, clearly established that the Court held as a matter of law that there was no evidence in the record that Maurice P. Koch ever acted in his own behalf. Note, also, the discussions with the Court which occurred at the time the exceptions to the challenged instruction occurred (R. 311, 312), at which time counsel for appellants stated:

“We also except with respect to the instruction given by the court that the jury may disregard all the activities of Maurice Koch if such activities involve only him, his own funds, it having been particularly held by this court that as a matter of law all of Maurice Koch’s activities in the motion picture business, the business of financing motion picture ventures, were for and on behalf of the partnership rather than his own behalf and a motion having been granted by reason thereof.

The Court. Very well.”

This error in charging the jury was magnified by the defense argument that Maurice P. Koch’s activities were in his own behalf, and not in behalf of the partnership, and that the jury should *not* consider his activities in determining whether or not the partnership had activity attributable to the particular trade or business. The Government thus took ad-

vantage of the benefits of the motion for a directed verdict which was erroneously granted by the Court on the basis that he was not, at any time, acting in his own behalf, and under these circumstances it was, indeed, unconscionable for the Government to then argue that Maurice P. Koch's activities were in his own behalf and that the jury must, therefore, disregard the same (R. 349, 352, 353, 354).

The error in the instruction is likewise emphasized by the fact that the partnership agreement (Appendix B) provides that Maurice P. Koch is in charge of all film business and that this phase of the business could be carried on in his own name. When the jury took the exhibits to the jury room, they found that all of the documents were in the name of Maurice P. Koch, and no doubt, under the Court's instruction, disregarded his constant activities as well as all of the documentation.

It is erroneous to instruct a jury when there is no evidence to support the theory of fact which the instruction assumes. See *Case of Tweed*, 83 U.S. 504, 16 Wall. 504, 21 L.Ed. 389 (1873); *McCarthy v. Pennsylvania R. Co.*, 156 F.2d 877 (7th Cir.), (1946).

(b) The Court instructed the jury (R. 301-302):

“... there is a presumption that the determination by the Commissioner of Internal Revenue that the plaintiffs were not engaged in the trade or business of financing motion picture ventures is correct. The burden is upon the plaintiff to overcome the presumption of the correctness of the Commissioner's determination by proving by

a preponderance of the evidence that they were engaged in the trade or business of financing motion pictures. By a preponderance of evidence is meant such evidence as when weighed with that opposed to it has more convincing force . . .", etc.

The instruction is clearly in error under the law. In the *absence of evidence* to the contrary, there is a presumption of correctness in favor of the Commissioner, but once evidence is introduced, the presumption fades and vanishes and the case is as wide open upon the evidence as though there had been no determination by the Commissioner, and the case must be decided "upon the evidence, and from it alone".<sup>4</sup>

In *J. M. Perry v. Commissioner*, 120 F.2d 123 (1941), C.C.A.9, this honorable Court stated, at page 124 with regard to such "presumption" as follows:

"This finding is presumptively correct, that is, until the taxpayer proceeds with competent and relevant evidence to support his position, the determination of the Commissioner stands. When such evidence has been adduced the issues depend *wholly* upon the evidence so adduced and the evidence to be adduced by the Commissioner. The Commissioner cannot rely upon his determi-

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<sup>4</sup>*Redfield v. Eaton* (D.C.) (1931), 53 F.2d 693, at p. 696:

"No one doubts that his decision is sufficient basis for the additional assessment and levy, thus casting on a plaintiff who brings the controversy into court the burden of proof upon all material allegations of the complaint. But that the Commissioner's decision, resting on evidence not presented to the court—in this case the defendant offered not a single witness—has the quality of probative evidence in determining the preponderance of evidence, is a proposition supported neither by authority nor reason."

nation as evidence of its correctness either directly or as affecting the burden of proof.” (Emphasis ours.)

Citing:

*Welch v. Helvering*, 290 U.S. 111, 115, 54 Sup. Ct. 8, 78 Law Ed. 212;

*Helvering v. National Grocery Co.*, 304 U.S. 282, 294, 295, 58 Sup. Ct. 932, 82 Law. Ed. 1346;

*Helvering v. Talbot Estates*, 4th Circuit (1940), 116 F.2d 160, 162.

This honorable Court clearly enunciated the rule in the case of *San Joaquin Brick Co. v. Commissioner of Internal Revenue*, 130 F.2d 220, C.C.A. 9 (1942), at page 225:

“It has often been pointed out that in claiming tax deductions the taxpayer must show clearly that he comes within the statute allowing such deductions. But once he presents competent and relevant evidence on every necessary element, the presumption of correctness of the Commissioner’s determination is no longer existent and the outcome of the case depends upon the determination of the trial body after the consideration of the evidence brought before it by both sides.” (Emphasis ours.)

And this honorable Court subsequently stated in *Hemphill Schools v. Commissioner of Internal Revenue*, 137 F.2d 961, C.C.A. 9 (1943) at pages 963, 964, as follows:



“Whether that determination was correct or incorrect was the principal, if not the sole, issue in the case. The burden of proving it incorrect rested on petitioner. Thus, if no evidence had been produced, the Board would have had to accept the determination; for, until evidence was produced, the determination was presumed to be correct. *Evidence was produced.* Some of the evidence produced by the petitioner tended to prove that its gains and profits were not permitted to accumulate beyond the reasonable needs of its business. Evidence having been so produced, *the presumption ceased, and thenceforth the issue depended ‘wholly upon the evidence’.* It thus became the duty of the Board to find *from the evidence, and from it alone*, whether petitioner’s gains and profits were permitted to accumulate beyond the reasonable needs of its business. No such finding was made. Instead, the Board treated the *presumption (which no longer existed)* as if it were evidence, weighed it against petitioner’s evidence and concluded that petitioner’s evidence did not ‘overcome’ it.

Decision vacated and case remanded, with direction to (1) find from the evidence, *and from it alone*, whether petitioner’s gains and profits were permitted to accumulate beyond the reasonable needs of its business.” (Emphasis ours, as well as this Court’s in certain instances.)

In *Lawrence v. Commissioner of Internal Revenue* (1944) (9th C.C.A.), 143 F.(2d) 456, this Court held that the presumption disappears when evidence is introduced sufficient to establish a prima facie case. We are constrained to observe that the policy of the

law cannot permit the extension of any rule whereby the person sued becomes the judge in the same lawsuit.

This unfortunate and devastating error in instructions occurred after the law upon the subject was argued to the Court and followed upon the heels of argument by the Government to the jury as follows (R. 344-345):

“In this case, and the Court will so instruct you, I believe, there is a presumption that the Commissioner of Internal Revenue’s determination is correct. You see, the plaintiff already had one crack at this case. He filed his claim for refund with the Commissioner of Internal Revenue and the Commissioner denied it.

Mr. Fink. Your Honor, I am going to enter an objection. We have not tried this case before. This is a lawsuit in itself.

The Court. This is the first time the case has been tried, counsel is correct, a claim has been filed.

Mr. Gillard. I will amend the word case and say ‘matter’. In connection with this claim for this deduction the matter has been previously presented by the plaintiff to the Commissioner of Internal Revenue and contrary to what Mr. Fink told you what the Commissioner of Internal Revenue said was ‘No, you do not have a business bad debt, you have a non-business bad debt’, and the Court will instruct you, I believe, that what a non-business bad debt means is that the parties were entitled . . . and in denying the claims made by plaintiffs, the Commissioner of Internal Revenue allowed each one of these plaintiffs on their tax returns for 1947 a deduction . . .”

And at the very closing final appeal, the Government stated to the jury:

“We submit to you, Ladies and Gentlemen, the finding of the Commissioner of Internal Revenue, who was a duly and regularly appointed executive officer of the Government, sworn to administer internal revenue laws, that his finding that this was a non-business bad debt, and under the Internal Revenue Code provisions that each of the seven parties to this action were entitled to take a deduction of \$1,000 per year against ordinary income for six years, was the correct conclusion in this case . . .” (R. 370-371).

By this argument, fortified by the erroneous instruction of the Court which followed, the jury were in effect told that their sworn officers at law had made a determination and knew more about the income tax system than the jury could ever know and that the determination was correct and remained correct and was sufficient to overcome all evidence offered against it.

The situation here is a far cry from the rule of this honorable Court that “the commissioner’s determination is no longer existent” . . . “the issue depended wholly upon the evidence” . . . “Find from the evidence, and from it alone . . .” etc. This erroneous instruction, combined with prejudicial misconduct of counsel, requires reversal.

(Note: The Court made its own findings and conclusions based upon the erroneous concept that the presumption continued, persisted, and pervaded all.)

2. The trial Court erred in its failure to give properly requested instructions necessary to a determination of the cause and in failing to give properly requested instructions upon plaintiffs' theory of the case.

In the absence of an agreement and other tangible evidence, the Courts have resorted to an analysis of the activities of the person involved to ascertain whether or not the transaction was related to a business.<sup>5</sup>

Not only did the four parties agree to engage in the business, but they actually so engaged in the busi-

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<sup>5</sup>In the absence of agreement, apparently the determination of whether one is engaged in a business turns upon the extent of his activities in the field in question.

*Dalton v. Bowers*, 287 U.S. 404, 53 S. Ct. 205, 77 L. Ed. 389;

*Burnet v. Clark*, 287 U.S. 410, 53 S. Ct. 207, 77 L. Ed. 397;

*Maloney v. Spencer*, 9th Cir., 172 F.2d 638;

*Daily Journal Co. v. Commissioner*, 9th Cir., 135 F.2d 687;

*Miller v. Commissioner*, 9th Cir., 102 F.2d 476;

*Commissioner of Internal Revenue v. Boeing*, 9th Cir., 106

F.2d 305, certiorari denied 308 U.S. 619, 60 S. Ct. 295, 84

L. Ed. 517;

*Harvey v. Commissioner*, 9th Cir., 171 F.2d 952;

*Fackler v. Commissioner*, 6th Cir., 133 F.2d 509;

*Kales v. Commissioner*, 6th Cir., 101 F.2d 35;

*Foss v. Commissioner*, 1st Cir., 75 F.2d 326;

*Commissioner of Internal Revenue v. Stokes' Estate*, 3rd

Cir., 200 F.2d 200;

*Campbell v. Commissioner of Internal Revenue*, 11 T.C. 510;

*Henry R. Sage v. Commissioner of Internal Revenue*, 15

T.C. 299.

Our search does not reveal any instance of similar tax contention where two or more people have agreed to engage in a certain business and have acted accordingly. The authorities hold that when a loss is suffered by reason of membership in a partnership, such loss is attributable to the trade or business of the partnership. It has been so held in instances upon termination of a partnership business when one partner remains indebted to the other and the indebtedness becomes uncollectible. In these cases the creditor was not engaged in the business of selling business interests or of terminating businesses. Nevertheless, the Tax Courts have held that losses resulting from an indebtedness by one partner to an-

ness pursuant to the agreement, and with a degree of regularity and continuity far and beyond that which is ordinarily to be found in the particular business in which they engaged.<sup>6</sup>

In view of the trial Court's rulings that appellants' written agreement, under which they at all times acted, did not, as a matter of law, establish that the particular loss was attributable to their trade or business, appellants presented evidence, and most of the record is devoted to a showing of a course of conduct by delineating activities.

We note that we are dealing with intangible "front money" activities in an intangible business where many ideas are started and few become finalized, where most efforts result in failure, and normally result in endless delays.

The defense argued that the jury should disregard all of the activities of the partnership devoted to the

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other are business bad debts, and therefore deductible in full (see *Davis v. Commissioner of Internal Revenue*, 11 T.C. 538. *Depuy v. Collector of Internal Revenue*, 55,081 Prentice Hall T.C. Memo., Docket No. 50,352 (1955).)

Corporations may deduct all of their losses including bad debts of every kind. Apparently, the theory underlying this rule is that clearly corporations are engaged in business. The same rule of reason should apply to a partnership. It would appear unnecessary to require a search for details, which under the clear concept of the law of evidence can only be admitted for the purpose of showing intention by proof of overt acts when in fact the parties have stipulated their intentions in formal writing and have acted accordingly.

<sup>6</sup>E.g., if four attorneys agree to practice law, they are clearly engaged in the law practice whether they ever conclude a case or not. Thus, also, if four persons agree, in writing, to erect suspension bridges and actually make numerous attempts to promote and sell the same, they are in that particular business, whether the bridges are ever built or not.

purpose of financing motion picture ventures unless such activities actually resulted in concluded substantial financing during the exact period in question (R. 369).

Appellants' proffered evidence, theory of the case, and argument were based upon the proposition that the activities, time, effort and money expended must be considered so long as the same related to the business of financing motion picture ventures and whether or not actual ventures were concluded and financed within the exact year in question. The ultimate question of fact is whether or not the loss occurred in the course of activities attributable to a particular trade or business.

Under these circumstances, appellants presented proper instructions upon the subject (R. 23, 24, 25, 26) and upon appellants' theory of the case. These instructions were proposed in order to give the jury some basis for its consideration of the substantial portions of the trial devoted to the activities of the partnership. The instructions were absolutely necessary as a basis for consideration of matters as follows:

1. The amount of time necessary to be devoted;<sup>7</sup>
2. Amount of capital necessary to be devoted;
3. Whether or not more than one business may be conducted by a partnership;

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<sup>7</sup>One may be engaged in a particular business although he devotes the major portion of his time and capital to another business (*Snyder v. Commissioner* (1935), 295 U.S. 134, 55 S. Ct. 737, 79 L. Ed. 1351; *Maloney v. Spencer* (C.C.A. 9) (1949), 172 F.2d 638).

4. Carrying on a business by devoting the time and attention of employees, agents, lawyers and representatives as distinguished from personal time;

5. That it was not necessary that transactions be *concluded* within the exact period in order that the devotion of time, effort and expenditures with respect thereto be considered; and

6. That it was not necessary that the transactions be concluded within the exact limits of the year 1947, in order for the jury to consider the time, effort and expenditures with relation thereto during the year 1947.

The failure to give the requested instructions (R. 23-26), or any of them, left the jury virtually uninstructed.

Each party is entitled to have his theory of the case submitted to the jury if there is any evidence to sustain it, and the theory of each party should be stated with equal completeness and clearness.

88 *C.J.S.* Trial Sec. 301b, pp. 816, 817;

53 *Am. Jur.* 487, 488, Trial Sec. 626;

*Aetna Life Insurance Co. v. Moore*, 231 U.S. 543, 34 Sup. Court 186, 58 L. Ed. 356 (1913).

In *Chicago & N. W. Ry. Co. v. Green*, 164 F.2d 55 (C.C.A. 8, 1947), the Court stated:

*“It has long been the rule that, as against a mere general or abstract charge, a party is entitled to a specific instruction on his theory of the case, if there is evidence to support it and if a proper request for such an instruction is made.”*  
(Emphasis ours.)

The Court did not give the jury any instruction upon which to predicate a finding or a "Yes" answer to the interrogatory propounded.

Also the following instructions consistent with the evidence and proper theory of the case was requested (R. 25) and refused.

"That if you should find that H. Koch & Sons, acting through one or more of its partners, or acting through persons, firms, corporations or representatives appointed by said partnership, regularly and continuously participated in the promotion and financing of motion picture ventures during the year 1947, then you must find that H. Koch & Sons was engaged in the business of financing and promoting motion picture ventures and that said business was regularly conducted."

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**D. THE COURT ERRED IN GRANTING A DIRECTED VERDICT (OR PARTIAL DISMISSAL) AGAINST MAURICE P. KOCH AND DAISY KOCH.**

It is not clear whether the Court granted a partial dismissal or directed verdict against Maurice P. Koch and his wife.

The trial Court, for the most part on its own initiative, granted a directed verdict, or dismissal against Maurice P. Koch with regard to a loss admittedly suffered by him in the sum of \$15,000.00 (R 292). All amounts were advanced by H. Koch & Sons, the co-partnership. After having advanced said funds, it appears that the partnership was short of funds



and Maurice P. Koch personally borrowed \$15,000.00 and contributed the same to the partnership (R. 287-8). The Court was in error in not finding that the \$15,000.00 loss was attributable to the partnership business. The error no doubt arose because of the failure of the Court to properly interpret the partnership agreement, as previously noted.

Even in the absence of the partnership agreement, the \$15,000.00 loss was a business loss.

In *Harding v. United States*, 113 Fed. Supp. 461 (1953), the plaintiff was a member of a partnership and personally borrowed funds and made a personal loan of the same to a third party with which to purchase a seat on the stock exchange for the purpose of promoting the interests of the brokerage partnership of which plaintiff was a member. The Court at page 463 of the opinion stated:

“Plaintiff’s sole purpose in borrowing the money was to promote the interests of this partnership. Plaintiff’s business was carried on through the partnership, and the loan therefore was made to promote plaintiff’s business. The loss of a portion of the loan was, therefore, directly attributable to the carrying on of plaintiff’s business.”

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**E. ERRORS IN RULING ON THE ADMISSIBILITY  
OF EVIDENCE.**

(1) The advancement of the funds lost were made more than ten (10) years prior to trial and the actual loss occurred more than nine (9) years prior to trial.

By agreement (Ex. 2, Appendix B) all activities of the partners in relation to motion picture finances were conducted by Maurice P. Koch. At the time of trial it became essential to determine the amount of time expended by him. The Court did not permit Maurice P. Koch to testify to the number of transactions in which he participated (R. 60). The Court held that it would be necessary to go into the details of each transaction without specifying any particular number or general continuity of time expended. The ruling was erroneous and eliminated the most pertinent and cogent testimony in the case. To make detailed moment by moment proof of activities and the contents of conversations and conferences conducted ten years prior to trial would result in hopeless confusion (e.g., if we were establishing the experience of a trial lawyer under the rule of evidence prescribed by the trial Court, we would be required to go through the exact details of each law suit in which he was ever engaged). Appellants were required, as a practical matter, to adopt some limits with regard to details, because to make proof in a trial Court of the details of activities which required more than one year for their occurrence, would, no doubt, require considerable unnecessary weeks and months to delineate by way of admissible testimony in a court room. Attempts by appellants to comply with this ruling did not fare well. Appellants sought to introduce documentation which resulted from interminable negotiations, conversations, discussions, trips, telephone calls, efforts of counsel and others and the

trial Court excluded the same. The jury were entitled to draw the reasonable inference from the very nature of the documentation, the many terms and provisions involved, the meticulous care in which the same were documented, the fact that in most instances several large feature films were projected and provided for, that the same required expenditure of very considerable time upon the part of persons acting for the partnership.

The documents were not offered to prove the truth of their contents, but were offered for the purpose of showing the time and effort expended and, further, to show the intention of the partnership as indicated by the overt acts of negotiations which resulted in the documentation. In particular instances, as will hereinafter be noted, documentation was excluded which had been fully executed and which was absolutely essential to explain the background and underlying reason for activities testified to and without which documentation the activities in and of themselves did not make sense.

Some of the instances of the exclusion of such documentation are as follows:

1. Exhibit 5, for identification (Appendix D) was repeatedly offered (R. 46, 210-212, 213-214). This was an Agreement between one, Coslow and United Artists Corporation for the production and distribution of "Copacabana" throughout the world. The due execution of the document was proved and it was likewise established that the picture "Copacabana" was pro-

duced and distributed pursuant to this agreement (R. 210-212). Since this was a fully and duly executed agreement pursuant to which the partners acted and the partners lost \$90,000.00, it was competent and relevant to show the following:

That Coslow contributed distribution facilities; that he had to be the principal stockholder of the corporation producing the same; and that he had to be the producer thereof. Therefore it became necessary for the partnership to provide the funds to activate Beacon Pictures Corporation, permitting Coslow to be the stockholder. The reason why the partnership became the beneficial owner of a substantial part of the picture "Copa-cabana" instead of co-producers and co-owners thereof is only explained by reference to this agreement. The agreement tends to establish the reason for activating the corporation for the production of films, and perhaps why corporations were organized. The agreement was necessary to supply the missing link in the testimony, and which was not otherwise admissible, to establish why appellants activated Beacon Pictures Corp., and to establish why appellants could not become the co-producers of the films.

A principal portion of the trial was devoted to inquiries as to why the partnership expended funds in activating Beacon Pictures Corporation with no other competent evidence to explain the reason for this expenditure except the terms of the said Agreement. The Court gave as reason for

its failure to admit the document in evidence that the names of H. Koch & Sons did not appear in the instrument (Exhibit 5 for identification) and the Court refused to hear from counsel thereon (R. 214). Appellants were third party beneficiaries to the Agreement, and in accordance with its terms, appellants (who were not named therein) would have received their income and benefits directly from United Artists (App. D).

Plaintiffs' theory of necessary proofs was as follows:

(i) The formal agreement of the parties entered into years prior to the loss in question and pursuant to which the partnership agreed to engage in the business of financing motion picture ventures as a business activity, and (ii) The numerous activities in regard to motion picture financing at the time in question; (iii) The substantial time expended by the personal activity of partners and the attorneys, agents and employees of the partnership.

When plaintiff sought to inquire as to the amount of time expended by directly inquiring into the fact in question, the Court erroneously sustained objection (R. 60):

“Q. (By Mr. Fink). Can you tell us approximately how many different deals were looked into by you over the period of the last six months of 1946?

Mr. Gillard. I object to that as vague and speculative, and calling for the opinion and conclusion of the witness.

The Court. I think in view of the objection he would have to give the individual contacts."

When plaintiffs made direct inquiry of a disinterested witness, who was present at almost every transaction, as to the amount of time spent by Mr. Koch in these activities to "your own personal knowledge" in the year 1947, this testimony was likewise excluded.

See (R. 245-246) "Q. (By Mr. Fink). So far as your own personal knowledge is concerned, with regard to the year 1947, approximately what part of Mr. Koch's time did he spend in connection with motion picture activities?

Mr. Gillard. I object to that as calling for the opinion and conclusion of the witness.

The Court. Sustained."

The manner of the trial judge suggested very strongly that extreme censorship would follow repeated attempts along this line. It was error to eliminate testimony upon time spent and number of transactions entered into during the periods in question. However, it was virtually impossible to overcome these errors when, in keeping with the Court's rulings, appellants sought to introduce the details relating to each separate transaction. Appellants offered documents prepared at the time and during the course of numerous transactions entered into in the period in question. Thus, appellants offered Exhibit 19 for

identification (Appendix E). This is an unsigned document which was negotiated by appellants during the year 1947 for the financing and production of a series of films. The record established that the parties to the agreement are well-known creative persons in the film industry. The offer of this document was specifically made for the purpose *only of showing the activities* of the partnership in financing motion pictures during the year 1947 and as part of the consistent and extended time and efforts expended, all to the point that the transaction in which the loss occurred was not an isolated instance of activity (R. 79-81). The document was prepared at the direction of the partnership; by counsel employed by the partnership; was reviewed by the partnership; was acceptable to the partnership; was part of the effort put forth in connection with the business of participating in the promotion and financing of motion pictures in the year 1947; was prepared in the course of that business; and all the shares of stock of the corporation involved (Ambassador Pictures) were acquired by the partnership (R. 78-85).

The offer of Exhibit 19 for identification was renewed (R. 84-85). The Court still refused to admit this and similar documents on the grounds that the same were not executed. The record was quite clear that documentation of this type was not offered to establish that a "package" was concluded, but was offered purely for the purpose of showing the time and effort expended. If this document and other sim-

ilar documents offered had been admitted by the Court, the jury could have reasonably drawn the inference, from the very nature of the transactions disclosed, that the preparation thereof was attended by negotiations, time, effort, attorneys' charges and other expenses. Certainly in determining whether or not a company is engaged in the business of financing, one should not be limited to consideration of activities only when funds are actually advanced.

The same situation applied with regard to Exhibit 21 for identification (Appendix F). The proposed employment contract between Ambassador Productions (the wholly owned corporation) and a director named Al Green (R. 84-85) which the Court excluded on the same ground, to wit, that it was not executed.

The same error occurred in connection with the offer of Exhibit 26 for identification (Appendix G), a contract negotiated in the exact period in question between Monogram Pictures Corporation and Ambassador Productions, Inc. (appellants' wholly owned corporation) for the financing, production and distribution of a series of films, together with a letter dated September 25, 1947, from Monogram Pictures Corporation. Although it was stipulated that the documents were prepared and received, the Court refused to admit the documents on the grounds that the same were not executed, and upon this premise the Court held that there was no foundation laid for their introduction (R. 99-100).



This document would have established that not only was someone doing something for the partnership in this field of endeavor, but reasonable minds could have drawn the inference that a great and extended effort was involved in arriving at the point of this documentation and that there were expenses and negotiations in connection therewith. It was clear that the document was offered for the purpose of proving activity and not to prove that a transaction was concluded. We submit that many transactions, which were intended to be concluded, could not be concluded due to the loss of the \$90,000.00 of funds in question. This loss was not realized at the time of these negotiations.

The Court likewise refused admission of Exhibit 29 for Identification (Appendix H), a letter of November 19, 1947, which established that negotiations and activities were continuing between the partnership and Monogram on that date (the prior documentation and correspondence, Exhibit 26 for Identification, having been dated September 25, 1947). Although it was stipulated that the letter was received, the Court nevertheless refused to admit the same. The grounds for its ruling are not clear unless it was because one of the attorneys to whom the letter was addressed was a director of the corporation which was wholly owned by the partnership; however, the record clearly established that the attorneys were acting for the partnership at all times and organized the corporation and

negotiated and prepared documentation only for and on behalf of the partnership (R. 78, 88-89, 109, 124). The Court's ruling, basically, was consistent with its opinion that such documentation should be excluded (R. 107-108).

The Court having ruled that only concluded transactions for financing need be considered, appellants attempted to offer evidence of actual advancement of funds and, among other things, established that a project was negotiated in 1947 for the financing of a series of army training films to be made by Apex Film Corporation. The first advancement of funds, however, occurred on January 26, 1948 (immediately following the close of the year in question). Appellants offered the cancelled check and details of the advances from the partnership, whereupon the Court ruled that details would not be admitted (R. 128-130). Objection was apparently made on the ground that the funds were expended after the close of the year 1947. The Court had ruled that only details of transactions were admissible for the year 1947 (R. 60, 245-246), and for the following month only general information. This evidence would tend to prove that the parties were engaged in the business at the end of the year 1947.

The Court likewise refused to admit Exhibit 24 for Identification which was offered to show extended negotiation over many months for the purchase of the story property "Hill of the Hawk" for the wholly owned partnership corporation, Ambassador Productions (R. 92-93). Funds were advanced and expended

in this project during the year 1947 and remained outstanding at the close of that year. The erroneous exclusion prevented proof of the commencement of negotiations and the time expended and intervening between initiation and closing of the "package".

Because "Hill of the Hawk" and other assets continued to be held by appellants for some years after expiration of the year 1947, and because defendants proved that "Hill of the Hawk" and Ambassador Productions was sold out some years later, appellants sought to offer testimony with regard to when the partnership discontinued its motion picture financing activities. This evidence was excluded on the erroneous ground that the questions called for a conclusion (R. 181, 182).

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#### F. ERRONEOUS FINDINGS.

(1) Finding No. 2 (R. 8) finds "Said Articles of Co-Partnership were amended by written agreement dated October 23, 1944" pursuant to which the partners agreed to also engage in the business of financing motion picture productions. "The said partnership agreement, as amended, has remained in full force and effect at all times herein mentioned." The Court followed this finding with its erroneous and confusing finding No. 5 which determines that "For the years 1945, 1946 and 1947 . . . — were partners in the business of manufacturing and selling luggage . . . " Thus, finding No. 2 and finding No. 5 are clearly in conflict.

Finding No. 5 is contrary to the basic and formal partnership agreement and the acts of the partners. The findings fail to find that the partnership had any activity in the business of financing motion pictures. If the Court had found that the number of activities was insufficient to constitute the doing of business, we would certainly differ; however, here in the face of overwhelming evidence the Court, in effect and tacitly, finds none. The record does not even leave open the possibility for consideration of the judgment in the light of appropriate findings.

(2) The complaint alleges and the answer admits the loss of the total sum of \$90,000.00 (*supra*). Finding No. 6 (R. 8-9) finds that only \$75,000.00 was lost which is contrary to the pleadings and issues as framed and upon which the cause was tried. The finding designates that a loan transaction occurred, whereas, in essence, the transaction was one by which the partnership acquired the largest block of ownership in the film of all participants by reason of its advancement of the \$90,000.00 which was lost and by reason of its activation of the corporation in whose name the picture was made.

(3) Findings Nos. 8 and 9 (R. 9-10) recite that the Collector of Internal Revenue "advised each of the plaintiffs that the claims for the year 1945 were denied, and that the claims for the year 1947 would not be allowed on the theory advanced to support the claims, but would be allowed as a non-business bad debt and not otherwise". This finding assumes that

plaintiffs are bound by the findings of the Collector of Internal Revenue and that this alleged presumption of correctness continues at the close of the lengthy trial to outweigh all evidence. At the close of the case, and after voluminous testimony, this "presumption of correctness" erroneously controls the determination of the cause. Since the determination of the Commissioner can no longer be considered as evidence in the cause, Findings 8 and 9 are not supported by the evidence.

(4) Finding No. 10 is in error. The Court here finds "Maurice P. Koch was not engaged in the business of financing motion picture ventures during the calendar year 1947". This fact was not in issue. The record is clear that all of his activities were in behalf of the partnership and never in his own behalf. The partnership agreement so provided (Exhibit 1, Appendix A; Exhibit 2, Appendix B). All of the funds, including the entire \$90,000.00 loss, was disbursed by the partnership upon the partnership bank account. Maurice P. Koch acted only for the partnership and not for himself and there is no evidence to the contrary (R. 43, 56, 57, 72, 76, 96, 97, 101, 112, 122-125, 191). The partnership agreement provided (Exhibit 2, Appendix B) that if one of the partners contributed more funds to the partnership than the others, such partner obtains a larger share of the profits and losses. Maurice P. Koch contributed an extra \$15,000.00 to the partnership funds and therefore was entitled to a larger share of the profits and losses. The

Court, however, interpreted the agreement erroneously and determined that Maurice P. Koch could not have the advantage of the additional loss unless he was personally (as distinguished from the partnership) engaged in the business of financing pictures, aside from his participation as a partner. There was absolutely no evidence in the record to show that he had ever engaged in his own behalf; and based upon its erroneous interpretation, the Court granted a nonsuit to the extent of his claim for the additional loss sustained.

(5) Finding No. 11 (R. 10) is in error in that the finding is predicated upon the assumption that the loss had to be related to a particular form of activity with third persons, (i.e. debt, joint venture, etc.). The only question at issue was whether or not the loss was related to a trade or business carried on by the plaintiffs. This must be determined by the plaintiffs' "trade or business", and is not at all determined by the particular form of the dealings with others. The plaintiffs already had a partnership pursuant to written agreement providing that they would engage in the business of financing motion picture ventures, and the pleadings admitted the loss of \$90,000.00 incurred in financing a motion picture.

(6) Finding No. 12 (R. 10) recites:

"12. The parties stipulated that the plaintiffs' rights to recover the alleged overpayments of taxes would require the jury to answer 'yes' to the following interrogatory submitted to them:

‘During the year 1947, was H. Koch & Sons regularly engaged in the business of financing motion picture ventures?’”

Finding 12 assumes that stipulations were entered into which were not entered into, and this finding is contrary to the express record. The record on the subject (R. 293) discloses the following:

“The Court. May it be stipulated by both parties that in view of the Court’s rulings up to this time, that the only issue to be presented to the jury is the special interrogatory which reads as follows:

‘During the year 1947 was H. Koch & Sons regularly engaged in the business of financing motion picture ventures? Yes—no.’

May that be stipulated?

Mr. Fink. So stipulated.

Mr. Gillard. So stipulated.

The Court. May it be further stipulated that thereafter, after such special interrogatory has been submitted to the jury, that all motions, issues and facts involved in the case are to be determined by the Court unless the parties stipulate as to such motions, issues or facts?

Mr. Fink. So stipulated.

Mr. Gillard. So stipulated.”

It was clear that only this one interrogatory could be agreed upon. All other matters were left for determination by the Court. The Court cannot avoid the necessity of finding fully and correctly upon the material issues involved. Thus, peculiarly, we have

no finding whatsoever that the partnership had any motion picture financing activities or business or the extent of the relationship to the business.

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#### G. ERRONEOUS CONCLUSIONS OF LAW.

The conclusions of law are erroneous in that they are based upon findings which are not supported by the evidence. They are apparently based upon stipulations which are not existent and contrary to the record. The conclusions in the first instance are based upon the presumption of correctness of the Commissioner of Internal Revenue's determination which is non-existent (see *supra*) after evidence was introduced. The conclusions are in error because the pleadings admit the loss of \$90,000. The conclusions of law are erroneous because they assume (Conclusion No. 4, R. 11, as well as other conclusions) that Maurice P. Koch individually (as distinguished from the partnership) made a loan. The entire \$90,000 was advanced by the partnership from partnership funds. All activities were conducted under the partnership agreement, by the partnership, and the loss was incurred by the partnership, as clearly demonstrated by the entire record, and not by Maurice P. Koch individually. This erroneous interpretation of the agreement by the Court, erroneous findings, erroneous partial dismissal, and now erroneous conclusions of law, have nullified the entire proceeding and prejudiced the determination of this cause.



#### H. THE JUDGMENT IS NOT SUPPORTED BY THE EVIDENCE.

(1) The judgment is based upon the determination by the jury of an answer to a special interrogatory. This answer to the interrogatory could only be based upon the erroneous instruction of the Court (R. 301, 302) that "There is a presumption that the determination by the Commissioner of Internal Revenue that the plaintiffs were not engaged in the trade or business of financing motion picture ventures is correct" and the further instruction that this presumption could only be overcome by a preponderance of the evidence. The findings of the Court are likewise predicated on this presumption (Finding No. 8, page 9) and the entire findings are based thereon. The conclusions of law likewise result from this alleged presumption and therefore are likewise erroneous.

It follows that the judgment is erroneous and in contravention of the express decisions of this Honorable Court (see 9th Circuit decisions, *supra*: *J. M. Perry v. Commissioner*, (120 F.2d 123 (C.C.A. 9)); *San Joaquin Brick Co. v. Commissioner of Internal Revenue*, 130 F.2d 220, at page 225 (C.C.A. 9); *Hemp-hill Schools v. Commissioner of Internal Revenue*, 137 F.2d 961, at pp. 963, 964 (C.C.A. 9).)

In said last case the Court stated: "Whether that determination (referring to determination by the Commissioner of Internal Revenue) was correct or incorrect was the principal, if not the sole, issue in the case." Peculiarly, this language applies with equal force to the instant case. It was practically the sole

issue relating to all facets of the instant cause and in all such facets the trial Court's rulings and determinations were erroneous with the result that the judgment is likewise erroneous.

No witnesses were called by the defense; no evidence was elicited by the defendant; all the evidence conclusively establishes that (a) plaintiffs had entered into a partnership agreement for the purpose of engaging in the business of financing motion picture ventures; (b) that they did so engage continuously during and throughout the entire period in question; (c) there is no evidence to the contrary in the absence of the alleged "presumption"; (d) the jury determined that the Commissioner of Internal Revenue knew more than they did about tax cases and found in accordance with the Commissioner's findings and not in accordance with the facts of the case; and (e) the Court took the answer to the interrogatory as the answer to the case, and assumed stipulations which did not exist for the purpose of resolving the entire matter based upon the erroneous determination by the jury.

The judgment is not sustained by the facts or the law.

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#### I. PREJUDICIAL MISCONDUCT OF COUNSEL.

Counsel for the Government told the jury that plaintiff was now engaged in a second trial of this matter; that plaintiff "already had one crack at this

case," (R. 344), and despite objections by plaintiff's counsel, Government counsel insisted upon telling the jury that the Commissioner of Internal Revenue had made a "determination" against the plaintiff. (R. 344.) These statements were fortified by further remarks of counsel that the Commissioner of Internal Revenue, who was sworn to uphold and preserve the people's rights, had determined the matter once and that the Commissioner knew more about tax determinations than the jury. (R. 371.)

Furthermore, in effect, Government counsel told the jury that plaintiff was attempting by surreptitious means to evade the "determination" of the Commissioner of Internal Revenue by laying down a "smoke-screen" (R. 346) and by attempting to "snow" the jury. (R. 366.)

Thus we have the attorney for the people (and therefore the representative of the jury) deliberately telling the jury to disregard all the evidence relating to transactions conducted by the plaintiff continuously and regularly and at great effort and cost, when said counsel knew that his statements were diametrically opposed to all the law on the subject and that in fact the jury was empaneled only to consider the extent of such activities, and certainly under all known law on the subject the jury should not have disregarded such activities.

**J. CONCLUSION.**

It is respectfully submitted that the judgment should be reversed and remanded to the trial Court for the computation of the amounts due plaintiffs; or, in the alternative, that judgment be reversed and the cause be remanded for trial.

Dated, February 7, 1958.

Respectfully submitted,

MAX FINK,

LEON SCHILLER,

*Attorneys for Appellants.*

**(Appendices Follow.)**

## **Appendices.**



## EXHIBITS WHICH ARE PART OF RECORD

Description	Page References to the Record			
	Exhibit Identified	Exhibit Offered	Exhibit Received	Exhibit Rejected
H. Koch & Sons Partnership Agreement dated December 31, 1941	R 35	R 35	R 35	
Amendment to Agreement of December 31, 1941	R 35	R 35	R 36	
Producers Syndicate Agreement	R 36	R 36	R 37	
Agreement between Copacabana, Inc. and Beacon Pictures, Inc. dated April 8, 1946	R 41	R 41	R 42	
Agreement between Coslow and United Artists Corporation	R 45	R 46 R 211 R 213 R 214		R 46 R 212 R 213 R 214
Photostat of check of April 25, 1946, drawn by H. Koch & Sons to order of David Sebastian in amount of \$15,000.00	R 47	R 47	R 47	
Letter of May 17, 1946, from David Hersch to H. Koch & Sons acknowledging receipt of funds	R 51	R 51	R 51	
Photostat of check drawn by H. Koch & Sons to order of David Sebastian in amount of \$2,500.00	R 53	R 53	R 53	
Letter dated July 31, 1946, from H. Koch & Sons to David Hersch	R 54	R 54	R 54	
Telegram addressed to Maurice P. Koch from David Hersch	R 54-5	R 55	R 55	
Photostat of check drawn by H. Koch & Sons to order of David A. Sebastian for \$50,000.00	R 55	R 55	R 55	

## Exhibits Which Are Part of Record (Continued)

Exhibit	Description	Page References to the Record			
		Exhibit Identified	Exhibit Offered	Exhibit Received	Exhibit Received
	Letter from Bank of America to David Hersch dated September 25, 1946	R 64-65	R 65	R 65	
	Promissory note of August 31, 1946, executed by Beacon Pictures Corporation and payable to order of Maurice P. Koch for amount of \$50,000.00	R 68	R 68	R 68	
	Check drawn by H. Koch & Sons to order of David Sebastian for \$30,000.00	R 68-69	R 69	R 69	
	Promissory note of October 17, 1946, executed by Beacon Pictures Corporation to order of Maurice P. Koch for amount of \$30,000.00	R 69	R 69	R 69	
	Letter of August 12, 1946 signed by David Hersch and David Sebastian, addressed to Murray P. Koch	R 69	R 70	R 70	
	Agreement between Murray P. Koch in behalf of H. Koch & Sons and Beacon Pictures Corporation, dated August 31, 1946	R 72	R 73	R 73	
	Supplemental Agreement between Murray P. Koch in behalf of H. Koch & Sons and Beacon Pictures Corporation, dated October 17, 1946	R 73	R 73	R 73	
	Check drawn by H. Koch & Sons to order of Beacon Pictures Corporation, dated November 22, 1946, for \$20,000.00	R 73-74	R 74	R 74	
	Unsigned document establishing venture for financing and production of a series of films, between Maurice P. Koch, in behalf of H. Koch & Sons, and other persons in the film industry	R 78, 80, 82	R 79, 80, 81, 82 84-85		R 80 85



## Exhibits Which Are Part of Record (Continued)

Description	Page References to the Record			
	Exhibit Identified	Exhibit Offered	Exhibit Received	Exhibit Rejected
Permit of Department of Investment, State of California, authorizing Ambassador Productions, Inc. to issue its shares of stock	R 83	R 83	R 83	
Unsigned Agreement between Ambassador Productions, Inc. and Alfred E. Green, dated April 28, 1947, providing for employment of Green	R 84, 85	R 84, 85		R 85
Document entitled "Mortgage," dated February 7, 1947, executed by Beacon Pictures Corporation in favor of Murray P. Koch	R 86, 87	R 87	R 87	
Articles of Incorporation of Ambassador Productions, Inc.	R 88	R 88	R 88	
Letter from Annie Laurie Williams to Max Fink, dated October 17, 1946, regarding Hill of the Hawk	R 92, 93	R 92, 93		R 93
Articles of Incorporation of Producers Finance Corporation	R 95, 96	R 95, 96	R 96	
Unsigned Agreement negotiated in 1947 between Monogram Pictures Corporation and Ambassador Productions, Inc. for financing, production and distribution of films, together with letter of transmittal dated September 25, 1947, from Monogram Pictures Corporation	R 99, 100	R 99, 100		R 99, 100
Letter of Harry Fox to Max Fink, dated July 3, 1947 relative to Fred Fisher story	R 104, 105	R 104, 105	R 105	
Letter of Harry Fox to Max Fink, dated September 29, 1947, relative to Fred Fisher story	R 105, 106	R 105, 106	R 106	
Letter of November 19, 1947, from Monogram Pictures Corporation to Max Fink	R 107, 108	R 107, 108		R 108

## Exhibits Which Are Part of Record (Continued)

Exhibit	Description	Page References to the Record			
		Exhibit Identified	Exhibit Offered	Exhibit Received	Ex Ref
	Check for \$7,000.00 dated December 3, 1947, payable to Ambassador Pictures Corporation and issued by Maurice P. Koch	R 114	R 114	R 114	
	Agreement between Scott O'Dell and Ambassador Pictures Corporation dated December 12, 1947	R 115	R 115	R 116	
	Check for \$5,000.00 dated June 8, 1948, to Max Fink from Maurice Koch and check for \$5,000.00 dated June 9, 1948, drawn on the trust account of Fink, Rolston, Levinthal & Kent, to Annie Laurie Williams, Inc.	R 116, 117, 118	R 117, 118	R 118	
	Two checks of May 10, 1948, one for \$4,500.00 and one for \$500.00, both drawn on trust account of Fink, Rolston, Levinthal & Kent, to Annie Laurie Williams, Inc. A check for \$8,000.00, dated July 9, 1948, drawn on same account to same payee	R 119, 120	R 119, 120	R 119, 120	
	Letter of July 8, 1948 from H. Koch & Sons to Max Fink and letter of July 9, 1948, in reply	R 122	R 122	R 122	
	Amended 1947 Partnership income tax return	R 186	R 186	R 187	
	Stock Permit of Producers Finance Corporation	R 195	R 195	R 195	

## Exhibits Which Are Part of Record (Continued)

Description	Page References to the Record			
	Exhibit Identified	Exhibit Offered	Exhibit Received	Exhibit Rejected
<b>Debtor's Exhibits:</b>				
Tax protest dated October 10, 1951	R 137			
H. Koch & Sons partnership return for 1946	R 141	R 141	R 141	
H. Koch & Sons partnership return for 1947	R 141	R 141	R 141	
Maurice P. Koch return for 1946	R 141	R 141	R 141	
Maurice P. Koch return for 1947	R 141	R 141	R 141	
Articles of Incorporation of Beacon Pictures Corporation	R 150, 151	R 150, 151	R 151	
Default Judgment against Beacon Pictures Corporation in favor of Maurice P. Koch	R 156	R 156	R 158	
Letter dated January 29, 1948, to Jack Chertok from Producers Finance Corporation	R 173	R 173	R 173, 174	
Check of Producers Finance Corporation to Max Fink dated July 8, 1948, for \$8,000.00	R 176	R 176	R 176	
Partnership Agreement between David Hersch and David Sebastian	R 248	R 248	R 248	
Certified copy of referee's claim register in bankruptcy proceedings of Beacon Pictures Corporation	R 260	R 260	R 260	



## Appendix A

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### PLAINTIFFS' NO. 1—IN EVIDENCE

THIS AGREEMENT entered into this 31st day of December, 1941, by and between REBECCA KOCH, MAURICE P. KOCH, HAROLD M. KOCH, and WILLIAM L. KOCH, all of the City and County of San Francisco, State of California,

### WITNESSETH:

WHEREAS, all of the parties hereto are brothers and sisters, and all are the recipients of a gift from their parents HERMAN KOCH and CELIA KOCH, the subject of which gift is that certain business known as HERMAN KOCH & SONS; and

\*            \*            \*            \*            \*            \*

Each and all of said parties agree, in consideration of the mutual promises and agreements from each of said parties, to the others, that his interest in said business shall continue only for such a period of time as he or she shall remain in active participation of said business, \* \* \* it being further understood that in the event any of said partners disassociates himself from said business voluntarily that his interest in said business immediately ceases and determines, and there shall be paid to said party for his interest in said business, regardless of the value of his interest therein, the sum of \$1000.00. It being further understood that in the event one of the parties hereto leaves said business, that the interests of said parties remaining shall be equal; it is further understood that the voluntary remaining away from said business for a

period of sixty days or more shall be deemed a prima facie withdrawal and disassociation from said business by the party so remaining away, and that at the expiration of the said sixty days his interest in said partnership business is subject to divestment.

\* \* \* \* \*

As compensation for services rendered by the parties in connection with said firm business, the salaries and drawings of said parties shall be as follows:

To REBECCA KOCH	\$70.00 per week;
To HAROLD M. KOCH	\$70.00 per week;
To WILLIAM L. KOCH	\$70.00 per week;
To MAURICE P. KOCH	\$100.00 per week

as salary, and \$100.00 per month as and for city and local sales expense, which said sum of \$100.00 per month is payable on the 1st day of each month in advance, \* \* \* In addition to the foregoing, the said Maurice P. Koch shall receive from the firm the sum of \$2100.00 annually as and for traveling and sales expense, which said sum is payable as needed by the said Maurice P. Koch while on the road traveling for said firm.

\* \* \* \* \*

It is further understood and agreed that all of said parties hereto shall devote all of their time to the interests of the said business and for the benefit thereof.

\* \* \* \* \*

In the event any dispute of any kind, nature or character, specifically including any dispute which

may arise as to any of the parties hereto losing his interest in said business by violation of the terms of this agreement, any and all such disputes shall forthwith, by any of the parties hereto or by any party interested in this or any other agreement made this date, or as heirs of any of the parties hereto shall be referred to MORRIS M. GRUPP for arbitration and decision.

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## Appendix B

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### PLAINTIFFS' NO. 2—IN EVIDENCE AMENDMENT TO AGREEMENT OF DECEMBER 31, 1941

THIS AGREEMENT entered into this 23rd day of October, 1944, by and between REBECCA KOCH, MAURICE P. KOCH, HAROLD M. KOCH AND WILLIAM L. KOCH, copartners, doing business under the fictitious firm name and style of H. KOCH & SONS, all of the City and County of San Francisco, State of California

#### WITNESSETH:

WHEREAS, it is the desire of the partners above named, and each of them, to enlarge the scope of their partnership business and activities and to amend the existing Articles of Partnership accordingly.

NOW, THEREFORE, in consideration of their mutual covenants and agreements the parties hereto, each for himself, agrees that the existing Articles of Copartnership, dated December 31, 1941, be amended to include therein the following:

1. The said partnership business will, in addition to engaging in those activities referred to in the existing partnership agreement, engage in the business of financing motion picture productions \* \* \*.

2. The assets of the partnership are to be available in the operation of this new business activity. It being understood further that nothing herein to the contrary withstanding, if any individual partner



or partners desires to advance any sums toward the abovementioned business activity over and above the sum advanced by this partnership that the profits realized on such sums advanced by the individual partners or the partnership shall be divided as follows:

(a) Moneys advanced by individual partners over and above the sum advanced by the partnership shall be first refunded to such partner or partners individually;

(b) The profits realized from that portion of the money advanced by the partnership or by the individual partners in equal sums each to the other shall upon realization of such profits become partnership assets;

(c) The profit on such sum or sums advanced by any one or more partners over and above that advanced by the other partner or partners shall belong to the individual partner or partners so advancing any excess;

(d) The losses on such sums advanced by the partnership or the sums advanced by individual partners to the extent that such sums so advanced by the individual partners are equal to that advanced by all the other partners shall be borne by the partnership and by the partners thereof equally. The losses on any sums advanced by individual partners over and above that advanced by the other partner or partners equally shall be borne wholly by said partner or partners so advancing such excess.

3. Maurice P. Koch is hereby appointed manager of that portion of the partnership business referred to in this Amendment and any expenses he may incur by reason of the management of this branch of the said business shall be borne by the said partnership in addition to any expenses heretofore provided in the original partnership agreement.

4. As such General Manager the said Maurice P. Koch is hereby authorized to deal in his own name with any person, firm or corporation with relation to the business herein referred to. It being understood and agreed that in so dealing in his own name the said Maurice P. Koch is acting as the agent of the said partnership and the agent of the individual partners thereto and that any funds received by him, any stocks or bonds or notes or other evidences of indebtedness, any contracts or licenses he may secure in his own name as a result of the proceeds of this partnership or the individual partners shall to the extent of the advance of moneys by this partnership or the individual partners be and remain the property of the partnership or the individual partners, notwithstanding that the same may on the written evidences of indebtedness or contracts stand in the name of Maurice P. Koch.

5. It being understood, however, in this connection that the said Maurice P. Koch will not enter into any transaction on behalf of said partnership without the consent of a majority of the partners and it being further understood that the said Maurice P. Koch is

to receive no increase in compensation for time devoted to this branch of the business.

EXECUTED by the parties hereto the day and year first above written.

Rebecca Koch

Maurice P. Koch

Harold M. Koch

William L. Koch

## Appendix C

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### PLAINTIFFS' NO. 3—IN EVIDENCE

THIS AGREEMENT entered into this 23rd day of October, 1944, by and between DAVE SEBASTIAN of the City of Beverly Hills, County of Los Angeles, State of California, and AL KANTROW, MAURICE P. KOCH, REBECCA KOCH, HAROLD M. KOCH, WILLIAM L. KOCH, JACK SILVERMAN, AL BACH, MAX GOTTLIEB, SAUL BAROFF, and MANUEL ROBINSON, all of the City and County of San Francisco, State of California, and HERMAN SALKIN of Redwood City, California, ROY HALLER, of Oakland, County of Alameda, State of California, MOE GOTTLIEB, of Ventura, California, MACK GILSON, of Oxnard, California, and HOBART W. RUDE, LOUIS LUBIN and SAM BRAUNSTEIN all of the City of Los Angeles, County of Los Angeles, State of California.

\* \* \* \* \*

Said partnership shall be known as "PRODUCERS SYNDICATE".

\* \* \* \* \*

3. The business of the partnership shall be to purchase an interest in the Sid Broad Production, "untitled," of a minimum of twenty per cent (20%) of the producer's share or cut in said production, and said money to be invested in this partnership is to be used specifically under the terms and conditions hereinafter set forth.

The further business of this partnership shall at the option of the partners, be the production of other motion pictures subsequent to the completion of the first picture by the Sid Broad Productions.

\* \* \* \* \*

11. It is understood and agreed that all of the monies of this partnership shall be placed under the exclusive control of Morris M. Grupp, who shall open a bank account under the name of this partnership, and shall have the right to draw upon said funds under the following conditions:

\* \* \* \* \*

*B.* The full sum to wit: \$50,000.00 shall be delivered to Dave Sebastian in full by the said Morris M. Grupp under the following conditions:

(1) When the said Morris M. Grupp is satisfied that the said Dave Sebastian has obtained, or will, simultaneously, upon the delivery of said money to the Sid Broad Productions, obtain the following contracts or assurances in writing:

(a) That full provisions have been made by the producer, to wit: Sid Broad, or by his agents, for the obtaining of any balance of monies necessary to produce the picture intended to be produced, over and above the \$50,000.00 to be delivered to the said Dave Sebastian. Said balance of such monies to be obtained by said producer either by deferments, loans or otherwise.

\* \* \* \* \*

## Appendix D

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### PLAINTIFFS' NO. 5—FOR IDENTIFICATION

#### AGREEMENT

Dated April 16th, 1946

By and Between  
Producer SAM COSLOW

with a place of business and address for all purposes hereunder at Hollywood, California

and

United

United Artists Corporation

a Delaware corporation, with its place of business and address for all purposes hereunder at 729 Seventh Avenue, New York City, New York.

\* \* \* \* \*

#### THE PRODUCER

The description and provisions concerning the Producer are set forth in Schedule "B" attached hereto.

#### SPECIFICATIONS AND DESCRIPTION OF MOTION PICTURES TO BE DELIVERED

The description of the motion pictures to be delivered hereunder, the conditions concerning such motion pictures, the type and quality of the motion pictures, the number of motion pictures and time of delivery of those motion pictures are set forth in Schedule "B".

## GRANT

The Producer grants to United and United accepts from the Producer the sole and exclusive right, license and privilege to exploit, distribute, exhibit and market, and cause to be exploited, distributed, exhibited and marketed the motion pictures specified herein in the entire world, including specifically the territories set forth in Schedule C hereto attached on both standard and sub-standard widths and both theatrical and non-theatrical, together with the right to re-issue same for a period of seven (7) years from the general release date of each said motion picture in the United States.

\* \* \* \* \*

1) THE PRODUCER represents and warrants that it owns the sole and exclusive license to produce a motion picture entitled "COPACABANA" which he will produce, and that Carmen Miranda, Dennis O'Keefe and Andy Russell will be starred in said motion picture, and when completed will deliver said picture to United for distribution which United agrees to accept for distribution.

2) The PRODUCER represents and warrants that he will have the controlling interest in the corporation which produces said picture.

\* \* \* \* \*

## PRODUCER'S RIGHT TO ASSIGN

a) Nothing herein contained shall be deemed to limit the right of the Producer to assign all of its right, title and interest in and to any motion picture, including the copyright thereto, the negative and positive copies thereof and that portion of the gross receipts payable to the Producer hereunder, to any company or corporation, provided, however, such company or corporation shall, at the time of such assignment be wholly owned or wholly controlled by Producer and provided, further, that should such company at any time cease to be wholly owned or wholly controlled by Producer, then and in that event the rights so assigned to it shall immediately revert to and revest in the Producer, and that such assignment shall be subject to such reversion and to the condition that the assignee company or corporation shall have no right to assign all or any right so assigned to it other than to the Producer. It is further agreed that any such assignment shall be subject to the rights of United hereunder and under any modifications thereof or amendments thereto, and shall not operate to relieve the Producer of any of its obligations hereunder.

b) Nothing herein contained shall be deemed to limit the right of the Producer to assign all of its right, title and interest in and to any motion picture, including the copyright thereto, the negative and positive copies thereof and that portion of the gross receipts payable to the Producer hereunder, to any bank or other person, firm or corporation, as collateral



security for a loan; provided, however, that any such assignment shall be made subject to the rights of United under this agreement and any modifications thereof or amendments thereto, and that it shall not operate to relieve the Producer of any of its obligations hereunder.

c) Nothing herein contained shall be deemed to prevent or prohibit the Producer from assigning to any person, firm or corporation all or any part of the Producer's interest in the receipts or proceeds of any completed motion picture. Any such assignment shall, of course, be made subject to the rights of the United under this agreement and any modifications thereof or amendments thereto, shall not operate to relieve the Producer of any of his obligations hereunder.

## Appendix E

---

### PLAINTIFFS' NO. 19—FOR IDENTIFICATION

THIS AGREEMENT, made and entered into this ..... day of ....., 1947, by and between MAURICE P. KOCH, hereinafter referred to as "KOCH", ALFRED E. GREEN, hereinafter referred to as "GREEN", DAVID A. SEBASTIAN, hereinafter referred to as "SEBASTIAN", and SIDNEY ROSS, hereinafter referred to as "ROSS."

This Agreement is made in contemplation of the following facts:

1) GREEN, SEBASTIAN and ROSS are officers and three of the directors of AMBASSADOR PRODUCTIONS, INC., a California corporation, hereinafter referred to as "CORPORATION."

2) That the sole stockholder of the said CORPORATION is MAURICE P. KOCH, who owns Five Hundred (500) shares of the common stock of said CORPORATION, having paid the sum of FIFTY (\$50.00) DOLLARS per share for said stock.

3) That the parties hereto are desirous of entering into an arrangement by which GREEN, SEBASTIAN and ROSS shall have an option to purchase a portion of the stock owned by KOCH.

NOW, THEREFORE, in consideration of the premises and the covenants hereinafter set forth, it is agreed as follows:

\* \* \* \* \*

## Appendix F

---

### PLAINTIFFS' NO. 21—FOR IDENTIFICATION

Los Angeles, California

April 28, 1947

Mr. Alfred E. Green  
Los Angeles, California

Dear Sir:

This will confirm your employment agreement with us as follows:

1. We hereby employ you to render your exclusive services for us as the producer and director for a period of three (3) years for and in connection with the preparation, production, direction and completion of not more than six (6) feature length motion picture photoplays in said period and in such other capacities relating to the preparation, production and completion of the photoplays as we may from time to time designate.

\*            \*            \*            \*            \*            \*

Your signature affixed at the place indicated will constitute this a binding agreement between us.

Very truly yours,  
AMBASSADOR PRODUCTIONS, INC.  
By .....

ACCEPTED AND AGREED TO:

.....  
Alfred E. Green

Appendix G

---

PLAINTIFFS' NO. 26—FOR IDENTIFICATION

September 25, 1947

Mr. Max Fink  
6253 Hollywood Blvd.  
Los Angeles, 28, California

Dear Max:

I am pleased to enclose for your inspection a draft of the proposed contract for two pictures to be supervised by Jack Chertok. I call your attention to the fact that the submission of the enclosure to you at this time is unofficial for the reason that this draft has not as yet been approved by Monogram.

After you have had a chance to go over this contract, please contact me so that we may discuss any questions which you may have concerning it.

Please excuse the delay in forwarding this instrument to you.

Kindest regards.

Sincerely,

Barney

BARNETT SHAPIRO - RESIDENT  
ATTORNEY

BS:jt

Enclosure

## AMBASSADOR PICTURES

Los Angeles, California

Gentlemen:

The following is our agreement:

## SECTION I

## PRODUCTION

1. You agree to produce and deliver to us for distribution by us two (2) motion picture photoplays. Said photoplays are hereinafter for convenience referred to as "the pictures".

\* \* \* \* \*

5. The first of the pictures shall be delivered to us not later than six (6) months after the date hereof, and the remaining picture shall be delivered not later than twelve (12) months from the date hereof.

\* \* \* \* \*

## Appendix H

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### PLAINTIFFS' NO. 29—FOR IDENTIFICATION

November 19, 1947

Mr. Max Fink

c/o Fink, Rolston, Levinthal & Kent

6253 Hollywood Blvd.

Los Angeles 28, Calif.

Dear Max:

I am pleased to re-submit herewith for your perusal a draft of the proposed contract by and between Ambassador Pictures and us with respect to the production and distribution of two photoplays.

In accordance with our discussion relative to changes, you will note that changes and revisions have been made on pages 5, 6, 8, 9, 10, 19 and 35. I believe that the enclosure now conforms to our discussions relative to this contract.

\* \* \* \* \*

## Appendix I

### PLAINTIFFS' NO. 24—FOR IDENTIFICATION

October 17, 1947.

Mr. Max Fink,  
6253 Hollywood Blvd.,  
Los Angeles, 28, California.

Dear Mr. Fink:      Re: HILL OF THE HAWK—by  
                                Scott Odell

\*            \*            \*            \*            \*            \*            \*

you asked me to give you the information that you need for drawing up the contracts for the motion picture sale of HILL OF THE HAWK:

As you know, the deal that I made with Mr. Chertok was for \$25,000.00 cash and five percent of the net profits of the picture. Of course by the net profits of the picture, we mean the amount remaining after the deductions for distribution charges and the negative cost of the picture, and the amount spent for prints and advertising.

\*            \*            \*            \*            \*            \*            \*

This contract may be assigned by Mr. Chertok to another person or corporation provided, of course, said person or corporation take over all of the obligations of the contract.

It is impossible for me to discuss all of the clauses in the contract until you draw the papers and send me a copy. If there is any point that needs clearing up at that time, we can make the necessary changes in the contract. But with this information you should be able to get the papers ready to send us next week. Please tell Mr. Chertok that the 8 copies of HILL OF THE HAWK he wanted are on the way to him.

\*            \*            \*            \*            \*            \*            \*

Annie Laurie Williams

## Appendix J

---

### PLAINTIFFS' NO. 13—IN EVIDENCE

H. KOCH and SONS

No. 742

Manufacturers of

The Original Aviation Luggage

73 Beale Street

San Francisco, California, Oct. 16, 1946

Pay to the order of

David Sebastian

\$30,000 00/100

The Sum of \$30000 and 00 cts

Dollars

Market-Ferry Office 11-153

American Trust Company

Head Office San Francisco

H. Koch and Sons

San Francisco, California

Rebecca Koch

\*            \*            \*            \*            \*            \*            \*



## Appendix K

---

### PLAINTIFFS' NO. 10—IN EVIDENCE

Murray P Koch Personal

Care Koch and Son 73 Beale St SFran=1946

Aug 4 PM 8 46

Kindly instruct David Sebastian return immediately.  
He bring 50,000. Will not give beacon until properly  
secured.

\* \* \* \* \*

Appendix L

---

PLAINTIFFS' NO. 12—IN EVIDENCE

\$50,000.00                      Los Angeles, Calif., August 31, 1946  
.....after date, for value received BEACON  
PICTURES CORPORATION promise to pay to  
MURRAY P. KOCH or order at Los Angeles, Cali-  
fornia Fifty Thousand and 00/100 Dollars.

\*                      \*                      \*                      \*                      \*                      \*

## Appendix M

---

### PLAINTIFFS' NO. 14—IN EVIDENCE

\$30,000.00      Los Angeles, Calif., October 17, 1946  
.....after date, for value received BEACON  
PICTURES CORPORATION promise to pay to  
MURRAY P. KOCH or order at Los Angeles, Cali-  
fornia Thirty Thousand and 00/100 Dollars.

\*            \*            \*            \*            \*            \*

## Appendix N

---

### PLAINTIFFS' NO. 16—IN EVIDENCE

THIS AGREEMENT entered into on the 31 day of August, 1946, between MURRAY P. KOCH, hereinafter referred to as "Lender", and BEACON PICTURES CORP., a corporation, hereinafter referred to as "Beacon".

\* \* \* \* \*

## Appendix O

---

### PLAINTIFFS' NO. 17—IN EVIDENCE

Mr. Murray P. Koch  
Los Angeles, California

Dear Mr. Koch:

This letter will supplement, amend and/or modify that certain agreement between us dated August 31, 1946, pursuant to which you loaned to us the sum of \$50,000.00. You have agreed to lend or advance to us concurrently with the execution of this supplemental agreement, and we hereby acknowledge receipt thereof, an additional sum of \$30,000.00, making a total loan of \$80,000.00; said additional \$30,000.00 to be used for the same purposes and pursuant to the same terms and conditions set forth in the aforesaid agreement dated August 31, 1946. Our agreement, therefore, is as follows:

\* \* \* \* \*

# Appendix P

---

## PLAINTIFFS' NO. 6—IN EVIDENCE

MAURICE P. KOCH

23815H

73 Beale Street

No. 0274

San Francisco, Calif., April 25, 1946

Pay to the order of

David A. Sebastian

\$15,000 00/100

Fifteen-thousand—————00/100

Dollars

Pacific National Bank

of San Francisco

H. Koch &amp; Sons

11-39 San Francisco, Calif.

Maurice P. Koch

\* \* \* \* \*

## Appendix Q

---

### PLAINTIFFS' NO. 8—IN EVIDENCE

H. KOCH and SONS

No. 23822

Manufacturers of

The Original Aviation Luggage

73 Beale Street

San Francisco, Cal., May 22, 1946

Pay to the order of

David Sebastian

\$2500 00/100

The Sum of \$2500 and 00 cts

Dollars

To

Pacific National Bank of San Francisco

H. Koch and Sons

11-39 San Francisco, Cal.

Maurice P. Koch

\*

\*

\*

\*

\*

\*

\*

Appendix R

PLAINTIFFS' NO. 10A—IN EVIDENCE

H. KOCH and SONS  
Manufacturers of  
The Original Aviation Luggage  
73 Beale Street  
San Francisco, Cal., Aug. 5, 1946

Pay to the order of  
David A. Sebastian  
The Sum of \$50,000 and 00 cts

No. 24004  
\$50,000 00/100  
Dollars

To  
Pacific National Bank of San Francisco  
H. Koch and Sons  
11-39 San Francisco, Cal. Rebecca Koch

\* \* \* \* \*

Stub:

Date	Description	Amount
8/5	In line with understandings arrived at re Copacabana picture	
		Total 50,000 00



**No. 15,645**  
**United States Court of Appeals**  
**For the Ninth Circuit**

---

HAROLD M. KOCH, BESSIE KOCH, WIL-  
LIAM L. KOCH, ROSE KOCH, REBECCA  
KOCH ABEL, MAURICE P. KOCH, and  
DAISY KOCH,

*Appellants,*

VS.

UNITED STATES OF AMERICA,

*Appellee.*

**On Appeal from the United States District Court  
for the Northern District of California.**

**APPELLEE'S BRIEF.**

---

CHARLES K. RICE,

Assistant Attorney General,

LLOYD H. BURKE,

United States Attorney,

LYNN J. GILLARD,

Assistant United States Attorney,

MARVIN D. MORGENSTEIN,

Assistant United States Attorney,

422 Post Office Building,

7th and Mission Streets,

San Francisco 1, California,

*Attorneys for Appellee.*

FILE

MAY -1 1958

PAUL P. O'BRIEN,



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No. 15,645

# United States Court of Appeals For the Ninth Circuit

---

HAROLD M. KOCH, BESSIE KOCH, WIL-  
LIAM L. KOCH, ROSE KOCH, REBECCA  
KOCH ABEL, MAURICE P. KOCH, and  
DAISY KOCH,

*Appellants,*

VS.

UNITED STATES OF AMERICA,

*Appellee.*

On Appeal from the United States District Court  
for the Northern District of California.

## APPELLEE'S BRIEF.

---

### JURISDICTION.

On July 5, 1955 in the United States District Court for the Northern District of California, Southern Division, the appellants filed an action for recovery of federal income taxes alleged to have been erroneously assessed and collected. Jurisdiction was invoked pursuant to 28 U.S.C. § 1346(a)(1) (1952). Trial by jury was demanded by the appellants, and the action was tried before the court and a jury on November 26, 27, 28 and 29. The jury returned a verdict in

favor of the appellee and on January 23, 1957 judgment was entered in favor of the appellee. A motion for new trial was filed and served on February 1, 1957, and denied on March 5, 1957. On April 18, 1957 the appellants filed a notice of appeal. Jurisdiction is invoked pursuant to 28 U.S.C. § 1291 (1952).

---

### **STATEMENT OF THE CASE.**

Appellants are a copartnership engaged in the business of luggage manufacturing. (Exhibit 1.) On October 23, 1944 the partnership agreement was amended to permit the partnership to engage in the business of financing motion pictures through direct participation, stock investment or loans. Two of the factors necessitating an amendment were the provisions in the original agreement that no partner could remain away from the business 60 days and that all of the partners must devote all of their time to the business. (Exhibit 1, pages 2 and 3.)

In April, 1946 Beacon Pictures Corporation, a corporation, was formed to engage in the production of motion pictures. The partnership did not engage in the organization of that corporation. (R. 147-148.) This action is based upon an alleged loss of \$90,000 through loans to Beacon Pictures Corporation. The loans were made in the following manner:

On April 25, 1946 the partnership issued a check payable to Mr. David Sebastian in the amount of \$15,000.00. (R. 47-50.) \$10,000.00 of this amount was



a loan to the partnership of David Hersch and Sam Coslow to set up Beacon Pictures Corporation. The remaining \$5,000.00 was a loan to Hersch and David Sebastian for expenses in commencing production. (R. 50.) An additional \$2,500.00 was loaned to Hersch and Sebastian for the same purpose. (Exhibit 8, R. 53.) The loan of \$10,000.00 to Hersch and Coslow was to be repaid by Hersch and Coslow when the picture was completed and sold. (R. 52.) The partnership thereafter drew checks in the amount of \$50,000.00 (Exhibit 10-A, R. 55-56) and \$30,000.00 (Exhibit 13, R. 68-69) to the order of Sebastian. The partnership received notes from Beacon Pictures Corporation for these two loans of \$50,000.00 and \$30,000.00. (Exhibits 12, 14; R. 68-69.) The partnership advanced an additional \$20,000.00 to Beacon Pictures Corporation, which amount was returned. (Exhibit 18, R. 74-75.)

The picture was completed, distributed, and was a failure. The partnership obtained a judgment against Beacon Pictures Corporation for \$80,000.00 (R. 157) and filed a claim against the bankrupt estate of Beacon Pictures Corporation. Subsequently it was determined that the loans to Beacon Pictures Corporation were worthless.<sup>1</sup> This is the loss which is the basis of the appellants' claim for refund. In addition, the taxpayers claimed as a loss the \$15,000.00 originally loaned to Hersch and Sebastian (see above)

---

<sup>1</sup>Appellants loaned \$97,500. Evidently \$7,500 of this represented loans made by Roy Haller (R. 277-279). This \$80,000 judgment against Beacon Pictures Corporation contained a \$5,000 claim of Roy Haller.

claiming that those loans were in fact made to Beacon Pictures Corporation.<sup>2</sup>

In addition to their isolated loan to Beacon Pictures Corporation, the appellants claim to have been engaged in the business of financing motion picture ventures. This claim of a business is based upon the following activity. Ambassador Productions, Inc. was formed and all shares of stock were issued to Maurice P. Koch. (R. 83.) This corporation purchased the rights to the book "Hill of the Hawk". (R. 93.)

A second corporation, Producers Finance Corporation, was formed in October, 1947. (R. 96.) Maurice P. Koch was president of that corporation from the moment of its inception. (R. 165.) As president of Producers Finance Corporation, Maurice P. Koch introduced Mr. Jack Chertok of Apex Film Corporation to the officers of the Pacific National Bank to secure a loan for Apex Film Corporation. (R. 174-175.) At this time, Apex Film Corporation had already been formed, and had made preparations to produce films. (R. 174.) Maurice P. Koch's only interest in this transaction was as a creditor of Apex Film Corporation. (R. 173-174.)

---

<sup>2</sup>In the complaint, the appellants alleged a \$90,000 loss. The appellee admitted this loss. In the course of the trial, the evidence disclosed that the loans were made to Hersch and Sebastian and Hersch and Coslow. The appellee moved the court to permit an amendment to the answer denying that the \$15,000 loss was suffered by the appellants. (R. 289-290.) This motion was denied. (R. 292.) Although the court failed to state the reason for this ruling, it was probably that since the court was directing a verdict as to the \$15,000 in dispute, there was no necessity for permitting an amendment to the answer in relation to that amount.

To further impress upon the jury that the appellants were in the business of financing motion picture ventures, there was testimony of numerous conversations, discussions, airplane journey and midnight phone calls by Maurice P. Koch. (See, for example, R. 202.) However, during much of this time, Maurice P. Koch was an officer and director of Producers Finance Corporation and Ambassador Pictures Corporation. (R. 167.)

The appellants filed income tax returns for the years 1945 and 1947. They thereafter amended these returns claiming a deductible loss for the year 1947 and a net operating loss carryback for the year 1945 arising out of the transaction involving Beacon Pictures Corporation. The claims for refund were denied upon the ground that that loss was a non-business bad debt. The appellants thereupon filed this action seeking refund of the tax paid.

In the complaint, the appellants also asserted that the loss was a loss arising out of a transaction entered into for profit within the meaning of Section 23(e) (2) of the Internal Revenue Code of 1939. Prior to trial counsel for the appellants agreed that this issue was being withdrawn from the action. Appellants state that no such stipulation was made. (See Appellants' Opening Brief, pages 58-59.) Unfortunately, the stipulation was not in writing. However, the instructions proposed by the appellants and the appellee, and the interrogatories submitted to the jury all omitted any reference to whether the transaction was in fact a transaction entered into for profit rather

than a debt. The conclusion is obvious that such a stipulation was made.

At the close of the evidence, the appellee moved (1) for a directed verdict as to all appellants and (2) to amend the answer to deny that Maurice P. Koch lost \$15,000 in addition to the \$75,000 lost by the partnership. The motion to amend was denied, and the motion for a directed verdict was granted against Maurice P. Koch and Daisy Koch for the \$15,000 which they claimed in addition to a share of the partnership loss. The jury then returned with a verdict that H. Koch and Sons was not regularly engaged in the business of financing motion picture ventures.

---

#### **SUMMARY OF THE ARGUMENT.**

1. (a) The appellants should not be permitted to allege error in the instruction that there is presumption that the determination by the Commissioner of Internal Revenue is correct and the appellants must overcome that presumption by a preponderance of the evidence. The appellants failed to object to the instruction when it was given. Therefore, they are precluded from challenging the instruction for the first time in this court.

(b) Assuming that the appellants may raise an objection to the instruction, the instruction was not erroneous. The instruction did not purport to give any weight as evidence to the Commissioner's presumption. The instruction stated that the appellants

had the burden of proving by a "preponderance of the evidence" that they were engaged in the trade or business of financing motion pictures. This did no more than state the burden placed upon a plaintiff in a civil action.

2. The directed verdict against Maurice P. Koch and Daisy Koch did not prejudice any of the appellants.

(a) The directed verdict did not prejudice the partnership. Maurice P. Koch testified that on all occasions he was acting on behalf of the partnership. (Appellants' Opening Brief, page 57.) None of the testimony of Maurice P. Koch was excluded. Thus, the jury considered all the testimony of Maurice P. Koch, in which he stated he was acting solely for the partnership, to determine whether or not the partnership was engaged in the business.

(b) Maurice P. Koch and Daisy Koch were not prejudiced by the directed verdict. Maurice P. Koch never claimed to have been acting for himself. He based his claim of a trade or business upon his identity with the partnership. Therefore, the directed verdict against Maurice P. Koch is immaterial since he is bound by the jury verdict that the partnership was not engaged in the business.

3. The court did not err in the instruction that the jury could disregard any of the activities of Maurice P. Koch where the jury believed he was acting on his own behalf and not on behalf of the partnership. Everything that Maurice P. Koch did, he did

in his own name. In fact, he advanced monies without the knowledge of the partnership. There was no evidence that the partnership acquiesced in all his activities. The ultimate issue must remain with the jury. The partnership agreement was only one of the factors they were warranted in considering to determine whether he was always acting for the partnership.

4. There was no error in the court's failure to give the three instructions requested by the appellants that in determining whether or not the appellants were engaged in the business of financing, the jury must consider all activity whether or not the transactions were actually concluded. The court permitted testimony of discussion, documents, telephone calls, all concerning activity where no proof was made that money was invested. In its charge, the court then stated to the jury that it could consider all of the time and effort devoted by the appellants. There was no restriction that actual financing must have occurred.

5. The argument to the jury by appellee's counsel concerning the activity of the Commissioner of Internal Revenue was not improper. Counsel was merely commenting upon the fact stated in the appellants' pleading. As such, it is proper comment to the jury.

6. The rulings of the court in relation to evidence received or excluded were proper. Documents excluded had no foundation and had no relevance to the trade or business of the partnership.

7. The jury's verdict is supported by the evidence. The existence of a partnership agreement alone cannot transcend any factual inquiry into whether or not the appellants actually did engage in a business. The jury observed the witnesses testify to the amount of time and effort expended in financing motion picture ventures. The trial court was liberal in permitting the jury to consider testimony of activity of separate and distinct corporate entities. The issue was a factual one and should be left to the jury to decide whether or not the appellants were engaged in the trade or business of financing motion picture ventures.

8. The court could have properly directed a verdict against appellants, but was generous in permitting the issue to be decided by the jury.

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### ARGUMENT.

1. **THE INSTRUCTION CONCERNING THE EFFECT OF THE COMMISSIONER OF INTERNAL REVENUE'S DENIAL OF THE REFUND CLAIM IS NOT GROUNDS FOR REVERSAL.**
  - (a) Neither of appellants' counsel objected to the instruction when it was given by the court. They are precluded from now raising it for the first time.

When the court concluded instructing the jury, counsel were given an opportunity to raise objections. (R. 306.) Counsel for the appellants excepted to instructions given and also took exception to the court's failure to give instructions. At no time did they raise

any objection to the instruction to which they now complain.

Rule 51 of the Federal Rules of Civil Procedure provides in part:

“No party may assign as error the giving or the failure to give an instruction unless he objects thereto before the jury retires to consider its verdict, stating distinctly the matter to which he objects and the grounds of his objection.”

Fed. R. Civ. P. 51.

And, Rule 18(d) of this court provides in part:

“When the error alleged is to the charge of the court, the specification shall set out the part referred to totidem verbis, whether it be in instructions given or in instructions refused, together with the grounds of the objections urged at the trial.”

Appellants' counsel failed to object as provided by Rule 51 of the Federal Rules of Civil Procedure, and accordingly are unable to comply with the requirements of Rule 18(d) of the Rules of the United States Court of Appeals for the Ninth Circuit.

This court has long required compliance with Rule 51 of the Federal Rules of Civil Procedure. A failure to object to the instruction when given precludes raising any objection to that instruction at the time of appeal.

*Persons v. Gerlinger Carrier Corp.*, 227 F.2d 337 (9 Cir. 1955);

*Lloy v. Pacific Electric Railway Co.*, 207 F.2d 662 (9 Cir. 1953);



*Wood Workers Tool Works v. Byrne*, 191 F.2d 667, 676 (9 Cir. 1951);

*Lynch v. Oregon Lumber Company*, 108 F.2d 283, 286 (9 Cir. 1939).

See also:

*Macartney v. Compagnie Generale Transatlantique*, 9 Cir. Feb. 28, 1958;

*United Press Associations v. Charles*, 245 F.2d 21 (9 Cir. 1957).

In *Macartney v. Compagnie Generale Transatlantique*, decided February 28, 1958, this court stated,

“Our view of the propriety of the court’s action in giving supplementary instructions in open court in the absence of counsel and any objection by such counsel makes it unnecessary to rest our affirmance upon the nature and content of the supplementary instructions.”

In a footnote to that statement, this court stated,

“In *Hutchinson v. Pacific Atlantic Steamship Company*, 217 F.2d 384 (1954), this court said: ‘As to the alleged error of the court in giving certain instructions: Appellant made no objection to the instruction she now complains of. In fact, she informed the court she had no objections. She should not now be heard to complain.’ [page 386.]”

Thus, as recently as February 28, 1958, the court reaffirmed its position that in order to raise an objection to an instruction, the appellant must have made formal objection to the instruction in the trial court.

- (b) Assuming that appellants may for the first time in this court inquire into the propriety of the instruction, the instruction does not constitute sufficient ground to reverse the jury's verdict.

The charge to which the appellants now complain was as follows:

“The burden of proof in this case is upon the plaintiffs to prove by a preponderance of evidence that the loan by plaintiffs to the Beacon Pictures Corporation was a loan made to plaintiffs’ regular trade or business. There is a presumption that the determination by the Commissioner of Internal Revenue that the plaintiffs were not engaged in the trade or business of financing motion pictures is correct. The burden is upon the plaintiff to overcome the presumption of the correctness of the Commissioner’s determination by proving by a preponderance of evidence that they were engaged in the trade or business of financing motion pictures.” (R. 301.)

The court then went on to discuss what it meant by evidence and a preponderance of evidence saying:

“By a preponderance of evidence is meant such evidence as when weighed with that opposed to it has more convincing force, and from which it results that the greater probability is in favor of the party upon which the burden rests. Preponderance of evidence means not the greater number of witnesses but the greater weight, probability, quality and a convincing effect of the evidence and proof offered by the party holding the affirmative as compared with any opposing evidence. If the scales of proof hang evenly the verdict should be against the party who has the burden of proof.

In determining whether any issue has been proven by a preponderance of evidence you should consider all of the evidence bearing either way upon the question, regardless of who produced it. A party is entitled to the same benefit from evidence that favors his cause or defense when produced by his adversary as when produced by himself.” (R. 302.)

The court did not instruct the jury that the presumption was to be considered as evidence in the case.

If appellants thought there was any error in this instruction they could easily have called it to the court’s attention. Instead they would now set aside a four-day trial on the basis of such an afterthought and on an alleged ground which obviously did not appear to them to be objectionable or prejudicial at the time the jury was charged. Appellants did not request explanation of the instruction as given. Instead, they remained mute.

In any event, the jury was not instructed that the presumption was to be given evidentiary weight, and the instruction did not convey that impression to them.<sup>3</sup>

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<sup>3</sup>A comparison of the instruction given by the court with instructions given by California courts in certain cases where a presumption does carry evidentiary weight will indicate this. For example, the inference of *res ipsa loquitur* is evidence to be considered by the jury. The jury is therefore charged: “An inference arises that the proximate cause of the occurrence was some negligent conduct on the part of the defendant. That inference itself is a form of evidence, and if none other exists tending to overthrow it . . .” California Jury Instruction Civil 206-B (4th Rev. Ed. 1956) . . . Similarly, in California there is a presumption that every person acts free of contributory negligence. Therefore, the jury is instructed as follows: “At the outset of the trial, each party was entitled to the presumption of law that

The trial court was clearly correct in instructing the jury as to burden of proof and preponderance of the evidence. In a refund suit it has repeatedly been held that the burden is on the taxpayer to establish his right to recover and the amount of the refund.

*Helvering v. Taylor*, 393 U.S. 507 (1935);  
*Maroosis v. Smyth*, 187 F.2d 228, 231-232 (9th Cir.), cert. denied 324 U.S. 814 (1951).

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**2. THE DIRECTION OF A VERDICT AGAINST MAURICE P. KOCH AND DAISY KOCH INDIVIDUALLY DID NOT PREJUDICE ANY OF THE APPELLANTS.**

The complaint sought recovery for taxes paid because of an alleged loss in the amount of \$15,000 individually on behalf of Maurice P. Koch and Daisy Koch. This \$15,000 allegedly represented loans by Maurice P. Koch to Beacon Pictures Corporation in excess of his proportionate share of the partnership loan. The court directed a verdict as to this amount. (R. 292.) The record warranted this ruling on any of the following grounds:

(1) These were not loans to Beacon Pictures Corporation but loans to David Sebastian;

(2) There was insufficient proof that these loans were made by Maurice P. Koch and were not, in fact, loans of the partnership; or

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every person takes ordinary care of his own concerns and that he obeys the law. These presumptions are a form of a prima facie evidence and will support findings in accordance therewith . . .” California Jury Instruction Civil 135 (4th Rev. Ed. 1956). These are instructions which tell the jury to give evidentiary weight to a presumption. The instruction given by the court in this action was not similar to these instructions and did not have the same effect.

(3) Maurice P. Koch never claimed to have been in the trade or business of financing motion pictures apart from his activities in the partnership.

Whatever the basis for the ruling, it is immaterial since no prejudice resulted to the appellants Maurice P. Koch and Daisy Koch or to the partnership H. Koch and Sons.

**(a) The partnership was not prejudiced.**

Maurice P. Koch was never acting on his own behalf. All of his activities were on behalf of the partnership. (R. 25, Appellants' Opening Brief 25, 33.) Although the court directed a verdict against Maurice P. Koch and Daisy Koch individually, the jury was permitted to consider all the activities of Maurice P. Koch in furtherance of the partnership business. The jury was instructed:

“Taxpayers may act through employees, agents and other persons, firms and corporations appointed by such taxpayers, and the acts of such employees, agents, or other persons, firms or corporations appointed by the taxpayer are in contemplation of law the act of the taxpayer. Thus, in considering the activities of the taxpayers in the instant case with relationship to the conduct, if any, of the business or enterprises, you are required to consider that the act of any such employees, agents, persons, firms or corporations appointed by them are in fact the acts and activities of the taxpayers.

“The authorized act or acts of any one partner of H. Koch and Sons in connection with the

partnership business or activities, are in contemplation of law the act or acts and activities of all of the partners." (R. 301.)

Thus, the jury was instructed to consider all the activities of Maurice P. Koch where it believed he was acting in furtherance of partnership interests in determining whether the partnership was engaged in the business of financing motion picture ventures. The partnership conducted its activities in the business of motion picture financing through the activities of Maurice P. Koch. Since the jury considered all of Maurice P. Koch's testimony, the partnership had the benefit of all evidence which was introduced.

**(b) Maurice P. Koch and Daisy Koch were not prejudiced.**

All of Maurice P. Koch's activity was on behalf of the partnership. He never purported to act for his own interests. Therefore, any finding on the partnership's business would be a finding upon the business of Maurice P. Koch individually.

Although the granting of a directed verdict may be error, if the jury verdict reaches the same result as the directed verdict, the parties can claim no prejudice.

*Buckeye Powder Company v. E. I. DuPont De Nemours, et al.*, 248 U.S. 55 (1918);

*Freeman v. Churchill*, 30 C.2d 453, 183 P.2d 4 (1947);

*Union Trust Co. v. Woodrow Mfg. Co.*, 63 F.2d 602 (8 Cir. 1933).

In *Buckeye Powder Company v. E. I. DuPont De Nemours, et al.*, 248 U.S. 55 (1918), the trial court directed a verdict in favor of certain defendants. The jury then returned a verdict in favor of the remaining defendants. The Supreme Court stated that since the liability of the defendant who was favored by the directed verdict was predicated upon the liability of the defendant who received the jury verdict, all defendants were exonerated by the jury verdict. The court held that in such a situation, an erroneous directed verdict does no harm.

The situation here is identical. Whether Maurice P. Koch was in the business of financing motion picture ventures depended upon whether the partnership of H. Koch and Sons was in the business of financing motion picture ventures. This result is necessitated by the appellants' position that Maurice P. Koch never acted on his own behalf, but on behalf of the partnership. Therefore, by its verdict concerning the partnership, the jury found that Maurice P. Koch was not in the business of financing motion pictures. If the court did not grant the directed verdict and deny recovery for the alleged \$15,000 individual loss, the jury verdict would have reached the same result. Therefore, any error in directing a verdict against Maurice P. Koch and Daisy Koch was not prejudicial.

3. THE COURT DID NOT ERR IN INSTRUCTING THE JURY THAT IT COULD DISREGARD ANY OF THE ACTIVITIES OF MAURICE P. KOCH AS PROOF THAT THE PARTNERSHIP WAS ENGAGED IN THE BUSINESS OF FINANCING MOTION PICTURES IF IT BELIEVED THAT IN A PARTICULAR TRANSACTION HE WAS ACTING ON HIS OWN BEHALF AND NOT ON BEHALF OF THE PARTNERSHIP.

The court instructed as follows:

“If you believe that Maurice P. Koch used his own money in any transaction and was acting therein in his own behalf and not on behalf of H. Koch and Sons, that transaction cannot be considered by you in determining whether the partnership of H. Koch and Sons was engaged in the business of financing motion pictures.”  
(R. 302.)

The appellants do not contend that this instruction does not properly state the law. (Appellant's Opening Brief, pages 31, 34.) Their complaint is that the instruction does not give sufficient weight to the testimony of Maurice P. Koch.

Maurice P. Koch testified that on every occasion he was acting on behalf of the partnership. Appellants allege error in the instruction that the jury was not compelled to believe him. The only basis for holding this instruction error is for the court to say that a jury is compelled to believe the testimony of an interested witness.

The jurors were instructed that they were the exclusive judge of the credibility of the witnesses. (R. 302.) The court further instructed them in the manner in which this credibility was to be determined. (R. 303-304.) If the jurors are not permitted to de-



termine the credibility of Maurice P. Koch, then they are compelled to accept as true the uncontradicted testimony of every witness. Such is not the law. See *Allen v. Matson Navigation Company*, 9th Cir., April 7, 1958.

Although Maurice P. Koch stated that he always acted on behalf of the partnership, other inferences may be drawn from the facts. For example, of the \$25,000 loaned by Producers Finance Corporation to Ambassador Pictures Corporation for purchase of the book "Hill of the Hawk", \$17,000 was repaid personally to Maurice P. Koch. (R. 177.) On cross-examination Maurice P. Koch divulged that the funds loaned were personal funds, that the partnership was short of money, and that the loan was never reflected on the partnership books. (R. 161.) Certainly the inference was permissible that the transaction was a personal transaction, and the appellee was entitled to an instruction which would permit the jury to draw that inference. In addition, the appellee impeached Maurice P. Koch in relation to his attempts to collect \$80,000 from Beacon Pictures Corporation. (R. 156-158.) In view of this impeachment, the jury should be permitted to evaluate the testimony of Maurice P. Koch to determine whether he was telling the truth.

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4. THE COURT DID NOT ERR IN REFUSING TO GIVE THE INSTRUCTIONS PROPOSED BY APPELLANTS NUMBERED 13 AND 15.

The instruction which apparently was appellants' proposed instruction number 13 stated:

“That in determining whether or not H. Koch and Sons was engaged in the business of financing motion picture ventures, you must consider, among other things, the amount of time and effort expended in that direction and such time and effort, if any, must be considered by you whether or not an actual venture was concluded.” (R. 25-26.)

The instruction which is apparently referred to as appellants' instruction number 15 was as follows:

“That in considering the question as to whether or not H. Koch and Sons devoted substantial time to the financing of motion picture ventures, you are required to consider all of their activities relating to that purpose, and all activities and efforts actually expended in attempting to negotiate for and in attempting to enter into financial transactions relative to the business of financing motion picture ventures must be considered by you upon this issue whether the same were concluded or not.” (R. 26.)

These instructions are confusing. The phrase “whether . . . an actual venture was concluded” is ambiguous and indefinite. There is no explanation in the instruction of how a venture is “concluded”. Therefore, the court could not give these instructions, since to do so would be error.

*United States v. Jones*, 33 U.S. 399 (1834);  
*Carpenter v. Connecticut General Life Ins. Co.*,  
 68 F.2d 69 (10th Cir. 1933).

But, assuming the instructions were not ambiguous, there was no error in refusing to include them in the

charge to the jury. Whether or not the activity constitutes a trade or business is a question of fact.

*Maloney v. Spencer*, 172 F.2d 638 (9th Cir. 1949).

To constitute a trade or business it must be shown that the activity was extensive, that it was regularly carried on, and that it constituted a major portion of the time, energy and effort of those who claim it as a trade or business.

*Towers v. Commissioner*, 247 F.2d 233, 235 (2nd Cir. 1957), cert. denied 355 U.S. 914 (1958);

*Hickerson v. Commissioner*, 229 F.2d 631 (2nd Cir. 1956);

*Giblin v. Commissioner*, 227 F.2d 692 (5th Cir. 1955);

*Commissioner v. Stokes Estate*, 200 F.2d 639 (3rd Cir. 1953).

The court instructed the jury:

“In determining that question you should consider all of the evidence which has been admitted in the case. The question of whether the debt is one the loss from the worthlessness of which is incurred in the taxpayer’s trade or business is a question of fact in each particular case. The statute does not give a definition for the word ‘business.’ Accordingly, in determining whether H. Koch & Sons was regularly engaged in the business of financing motion picture ventures you should consider the word ‘business’ to have its ordinary, common and accepted meaning. A taxpayer may engage in or regularly conduct one or several businesses at the same time. The amount

of time as well as the proportionate amount of capital devoted to a particular business are each factors among other factors to be considered in determining whether or not one is regularly engaged in a particular business.

“If a taxpayer regularly and continuously participates in business ventures in which he is not only financially interested but to which he devotes a substantial part of his time, such activities may make such ventures a trade or business of the taxpayer. Isolated or infrequent transactions of a taxpayer in any field do not constitute a trade or business within the meaning of the Internal Revenue Code.

“In determining whether an activity of a taxpayer is a trade or business you should consider among other things how extensive was the activity, the financial investment therein, whether it was regularly carried on, and whether the activity occupied a substantial portion of the time, energy and effort of the taxpayer.”

This was a proper statement of the applicable legal principles. The court advised the jury that the amount of time spent was a factor to be considered in determining whether the partnership was engaged in a trade or business. The jury was further advised that it was to consider whether the activity was regularly carried on and whether it occupied a substantial portion of the time, energy and effort of the partnership. Under this instruction, the jury was advised to consider all activities of the taxpayer, regardless of whether financing was accomplished.

And this was the nature of the evidence which the court permitted to go to the jury. Appellants, over

objection by the appellee, were permitted to introduce evidence relating to numerous phone calls, conversations, and documents relating to activities of the appellants in matters where no financing was ever accomplished.

Evidently the appellants complain that the court did not specifically instruct the jury that the appellants could be in the business of financing "whether or not an actual venture was concluded." (R. 26.) Although the court did not use the appellants' language, the import of its charge to the jury was that the jury should consider all activity of the taxpayers whether or not financing was concluded. Nothing further was required. "A judge is not bound to adopt the categorical language which counsel choose to put into his mouth. Nothing could be more misleading. If the case is fairly put to the jury, it is all that can reasonably be asked."

*Ayers v. Watson*, 137 U.S. 584, 601 (1902).

But even if this court determines that the instructions did not permit the jury to consider activities where financing was not actually accomplished, the appellants were not entitled to such an instruction. Where the business is that of lending money, the important issue is whether or not the taxpayer had actually loaned money.

*Commissioner v. Smith*, 203 F.2d 310 (2nd Cir. 1953), cert. denied 346 U.S. 816;

*Pokress v. Commissioner*, 234 F.2d 146 (5th Cir. 1956);

*Friedman v. Delaney*, 171 F.2d 269 (5th Cir. 1948).

Thus, whether loans were made was a factor to be considered in determining whether the taxpayers in the above cases were in the business of making loans. Here, therefore, whether any financing was actually done should be a factor to be considered in determining whether the appellants were engaged in the business of financing motion pictures. Accordingly, the appellants were not entitled to the instructions which advised the jury that whether or not actual financing was done was immaterial.

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**5. ARGUMENT OF THE APPELLEE'S COUNSEL WAS  
NOT PREJUDICIAL MISCONDUCT.**

Counsel for the appellee stated to the jury:

“You see, the plaintiff already had one crack at this case. He filed his claim for refund with the Commissioner of Internal Revenue and the Commissioner denied it.”

Upon objection by counsel for appellant, the court instructed the jury: “This is the first time the case has been tried and counsel was correct. A claim has been filed”. Counsel for the appellee then stated that the “matter had been presented to the Commissioner of Internal Revenue.” (R. 344.) Thus, the jury was not told that the case had been tried previously.

The jury was told that the defendant, through the Commissioner, believed this was a non-business bad debt. This was the fundamental issue in the action. The appellants claimed a business loss, and the appellee claimed it was a non-business bad debt. Appel-

lee's counsel merely informed the jury of the appellee's contentions.

In the complaint, appellants alleged: "The Commissioner of Internal Revenue, through the office of the Regional Commissioner of Internal Revenue, notified plaintiff on September 10, 1954 that said \$9,375 chargeable loss was a 1947 loss but that in his opinion the loss was a non-business bad debt and was therefore a capital loss and thus was deductible by petitioner in 1947 only in the amount of \$1,000." (Supp. R. 386.) The complaint was replete with similar statements. (Supp. R. 388, 390, 392-93, 394, 396, 398, 400, 402, 404, 406, 408-09, 411, and 413.) Appellee's counsels' remarks were merely stating what the appellants had alleged in the complaint. In *Knight v. Russ*, 77 Cal. 410, 19 Pac. 698 (1888), plaintiff's counsel read parts of the complaint to the jury. The Supreme Court of California there stated: "And if in the progress of the argument, counsel desires . . . to further call the attention of jury to the facts alleged, there can so far as we can see, be no impropriety in doing so."

*Knight v. Russ*, 77 Cal. 410, 414, 19 Pac. 698, 700 (1888).

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#### 6. THE COURT DID NOT ERR IN ITS RULINGS ON ADMISSION OF EVIDENCE.

Plaintiffs offered an agreement between one Sam Coslow and the United Artists Corporation. (Exh. 5, Appellants' Opening Brief, Appendix D.) It con-

tained no reference to the appellants. (R. 213.) The only purpose of the agreement was to show the activity of other persons. Appellants' counsel stated: "It is part of the overall picture, to show the contribution of each person toward the entire pot that makes the independent picture." (R. 211-212.) The agreement did not relate to any activity of the appellants, and therefore, had no bearing upon whether the appellants were in the business of financing motion pictures. In any event, there was sufficient testimony of the existence of the agreement. (R. 45-46.) Thus, appellants' counsel were not prejudiced by the failure to admit the document.

Plaintiffs' offers of Exhibits 19, 24, 26, and 29 were refused by the court. These exhibits all related to activity of third persons and Ambassador Pictures Corporation. Ambassador Pictures Corporation was an independent entity, whose activities are not the activities of the appellants.

*Dalton v. Bowers*, 287 U.S. 404 (1932);

*Burnett v. Clark*, 287 U.S. 410 (1932);

*Skarda v. Commissioner of Internal Revenue*,  
250 F.2d 429 (10th Cir. 1957).

The exhibits, therefore, are not relevant to show the activities of the appellants.

But, in any event, whether or not the documents are relevant, the appellants were not prejudiced by their exclusion. The documents were not offered for the truth of the statements contained in them, but were offered to prove the fact of the documents themselves—they were offered as proof of activity. With



the offer of each document, Maurice P. Koch testified that he had authorized or directed the preparation of the document as part of his activity. Although the document was not admitted in evidence, the very fact of the activity was in evidence by testimony of Maurice P. Koch.

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**7. THE JURY VERDICT WAS NOT CONTRARY TO THE  
WEIGHT OF THE EVIDENCE.**

The issue was whether the appellants were in a trade or business within the meaning of the Internal Revenue laws. The appellants alleged that they were in the business of financing motion picture ventures. Whether or not the activity constituted a trade or business was a question of fact.

*Higgins v. Commissioner*, 312 U.S. 212, 217 (1941).

Here, the appellants amended their partnership agreement to provide that they would be in the business of financing motion picture ventures. Appellants contend that the existence of the partnership agreement compelled the finding that they were in fact engaged in the business of financing motion pictures. However, it would seem that the existence, or non-existence of an agreement to engage in a business is merely a factor to be considered in determining whether the parties are actually engaged in the business.

In *Skarda v. Commissioner*, 250 F.2d 429 (10 Cir. 1957), the taxpayers were a partnership which engaged in various activities. One of the activities was the publication of newspapers. Subsequently, the

partners became the sole owners of a corporation which undertook the publishing business. However, there were no meetings of stockholders, no by-laws, no election of officers, no minute books, no corporate stock, and no property was formally transferred by the partnership to the corporation. Thereafter, the partnership made loans to the corporation which became worthless. The partnership claimed business deductions for these losses. The partnership contended that since it was the sole shareholder of the corporation, and that the corporation was merely organized to carry on business of the partnership and had not complied with the laws of the State relative to the formation of corporations, the losses were in fact business losses of the partnership.

The Court of Appeals for the Tenth Circuit denied this contention. It held that the losses had no relation to any business of the partnership. Thus, the fact that the partnership had agreed to engage in the publishing business was immaterial without further proof of actual publication.<sup>4</sup>

The appellants here demanded a trial by jury upon the issue of whether or not they were engaged in the business of financing motion picture ventures. The issue for the jury was whether evidence introduced by appellants showed sufficient activity to constitute a trade or business. The jury determined that it did not. This verdict should not be set aside.

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<sup>4</sup>Although in the *Skarda* case, the court did not state that the partnership agreement was in writing, this would appear to be immaterial. Whether the agreement is in writing or oral is not relevant if the existence of the agreement is accepted.

8. THE EVIDENCE WARRANTED THE JURY VERDICT. THE COURT CORRECTLY MIGHT HAVE DIRECTED A VERDICT AGAINST THE APPELLANTS AND WAS GENEROUS TO THEM IN LEAVING THE QUESTION TO THE JURY. ACCORDINGLY, APPELLANTS HAVE NOT BEEN PREJUDICED BY THE JURY VERDICT.

(a) The means by which the partnership attempted to place itself in the business of financing motion pictures was through the activity of Maurice P. Koch. Although Maurice P. Koch was a partner in H. Koch and Sons, the partnership cannot adopt his activity to establish the business of financing motion pictures.

Maurice P. Koch was also an officer and director of Ambassador Pictures Corporation and Producers Finance Corporation. He testified extensively to negotiations for the purchase of "Hill of the Hawk" by Ambassador Pictures Corporation. However, financing the purchase of "Hill of the Hawk" for Ambassador Pictures Corporation was not done by Maurice P. Koch on behalf of the partnership, but was done by Maurice P. Koch on behalf of Producers Finance Corporation. (R. 167.) It was Producers Finance Corporation which loaned \$25,000.00 to Ambassador Pictures Corporation for purchase of "Hill of the Hawk", not Maurice P. Koch, or the partnership. (R. 176-177, Defendants' Exhibit "I".) In all the dealings by Maurice P. Koch in relation to the purchase of "Hill of the Hawk", he was not acting as a partner in H. Koch and Sons, but he was acting as the shareholder, officer and director of Ambassador Pictures, Inc. (R. 164-165.) Through his own testimony, it is evident that Maurice P. Koch was acting in his capacity as shareholder and director

of Ambassador Pictures Corporation and Producers Finance Corporation.

Further evidence that the loan to Ambassador Pictures Corporation was made by Producers Finance Corporation and not the partnership was the check to Ambassador Pictures. The maker of the check was Producers Finance Corporation. (Defendants' Exhibit I, R. 176-177.) The financing, therefore, could not have been by the partnership.

The corporation is regarded as an entity distinct from its shareholders, directors or officers. Relying upon this principle, the Supreme Court of the United States has held that the business of the corporation is not the business of the shareholder, officer or director.

*Dalton v. Bowers*, 287 U.S. 404 (1932);

*Burnett v. Clarke*, 287 U.S. 410 (1932).

See also:

*Skarda v. Commissioner*, 250 F.2d 429 (10th Cir. 1957);

*Commissioner v. Smith*, 203 F.2d 310 (2nd Cir. 1953), cert. denied 346 U.S. 816;

*Commissioner v. Stokes Estate*, 200 F.2d 637 (3rd Cir. 1953);

*Van Dyke v. Commissioner*, 63 F.2d 1020 (9th Cir. 1933), affirming 23 B.T.A. 946 (1931), affirmed 291 U.S. 642 (1933).

The major portion of Maurice P. Koch's activity was devoted to his activities as shareholder and director of Ambassador Pictures Corporation and Producers Finance Corporation. (R. 167.) This activity cannot be considered in determining whether H. Koch

and Sons was engaged in the business of financing motion pictures. If the activity is excluded, there was not sufficient evidence of activity by the partnership to sustain a finding that they were in the business of financing motion picture ventures.

(b) It is appellants' contention that although Maurice P. Koch may have been acting on behalf of Ambassador Pictures Corporation and Producers Finance Corporation, these corporations were the agents of the appellants. [See Appellants' Opening Brief 51-54 and proposed Instruction No. 9 (R. 24) which was given by the Court (R. 301).] To be considered an agent, the corporate business purpose must be carrying on the duties of an agent.

*National Carbide Corporation v. Commissioner*,  
336 U.S. 422, 437 (1949).

Here, the corporations were not formed to act as agents, but were formed for the specific purpose of producing motion pictures (R. 82) and financing motion pictures (R. 95). The activities of these corporations cannot be ascribed to the partnership.

*National Carbide Corporation v. Commissioner*,  
336 U.S. 422 (1949);

*Moline Properties, Inc. v. Commissioner*, 319  
U.S. 436, 439 (1945).

If the activities of Ambassador Pictures Corporation and Producers Finance Corporation are excluded, there was not sufficient evidence of activity by the appellants to sustain a finding that they were in the business of financing motion picture ventures.

(c) The activity of financing motion picture ventures cannot be a trade or business within the meaning of the Internal Revenue laws.

The business of the corporation cannot be the business of the shareholders or directors. A taxpayer associated with many corporations cannot rely on the activities of the organization, but must establish his own activity apart from the organization's to prove a trade or business.

*Dalton v. Bowers*, 287 U.S. 404 (1932) ;

*Burnett v. Clarke*, 287 U.S. 410 (1932).

In *Commissioner v. Smith*, 203 F.2d 310 (2nd Cir. 1953), cert. denied, 346 U.S. 816 (1953), the Second Circuit refused to recognize investment management and other forms of financing as a trade or business.

This Court has taken a similar position. In *Ada v. Van Dyke*, 23 B.T.A. 1953, the taxpayer was engaged in development and promotion of town sites. The taxpayers financed the development of the town sites, utility companies and other forms of municipal improvements. The loss in question resulted from a loan to a corporation to promote the development of land sites and utilities. The Board of Tax Appeals held that the loss did not result from a trade or business. This Court affirmed, 63 F.2d 1020 (1933), citing *Burnett v. Clarke*, supra, and *Dalton v. Bowers*, supra. The judgment was affirmed by the Supreme Court of the United States, 291 U.S. 642 (1933). There, the investment and loans were made with the purpose of promoting, financing and organizing the utility companies and real estate improvement land.

See also:

*Hickerson v. Commissioner*, 229 F.2d 631 (2nd Cir. 1956);

*Towers v. Commissioner*, 247 F.2d 233, 235 (2nd Cir. 1957), cert. denied 355 U.S. 914 (1958).

The import of these decisions is that one who is instrumental in the formation of corporations and suffers a loss through a loan to one of the corporations, has not suffered a loss arising out of a trade or business. If these cases are to be followed, the activity of the appellants was not a trade or business.

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### CONCLUSION.

The judgment should be affirmed.

Dated, April 23, 1958.

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Assistant United States Attorney,

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(Case 10)

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No. 15,645

United States Court of Appeals  
For the Ninth Circuit

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HAROLD M. KOCH, BESSIE KOCH, WIL-  
LIAM L. KOCH, ROSE KOCH, REBECCA  
KOCH ABEL, MAURICE P. KOCH, and  
DAISY KOCH,

*Appellants,*

VS.

UNITED STATES OF AMERICA,

*Appellee.*

On Appeal from the United States District Court  
for the Northern District of California.

APPELLANTS' REPLY BRIEF.

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FILED

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## APPELLANTS' REPLY BRIEF.

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### ARGUMENT.

#### I.

**THE ERRONEOUS INTERPRETATION OF THE TERM "ENGAGE  
IN THE BUSINESS OF FINANCING MOTION PICTURE PRO-  
DUCTIONS".**

The errors during trial, now emphasized by Ap-  
pellee's Brief, resulted from an erroneous interpreta-  
tion of the phrase taken from the partnership agree-  
ment (Appellants' Brief, Appendix B), i.e., "... en-  
gage in the business of financing motion picture pro-  
ductions . . ." The term "finance" and the corre-  
sponding term "financier" must be defined as the con-

duct of financial affairs and negotiations respecting the same. Definition must include negotiation for participating interests, profits, and other considerations which prompt and promote all business activity.

At the time of trial, as well as in its brief, appellee asserted that engaging in the business of financing motion picture ventures means only the making of loans, and that only consummated loans are relevant for consideration in determining whether or not the loss in question resulted from an isolated transaction, as distinguished from the conduct of business. Unfortunately, appellee was substantially supported in its views by the trial Court.

In every motion picture venture appellants negotiated for substantial participation by way of ownership, and assignments of income and profits. Each transaction contemplated profit and ownership participations, as distinguished from simple interest for the funds advanced. Thus, appellants became the assignee and largest owner of the profits and benefits of the picture "Copacabana" from which the \$90,000.00 loss resulted. We do not deem it necessary that the respective transactions receive definite labels or precise legal definitions. See *Nelson v. Abraham*, 29 Cal. 2d 745, 177 P. 2d 931; *Hyman v. Hyman*, 98 C.A. 2d 463, 220 P. 2d 623. It is sufficient to note that in each instance it was contemplated that the partnership would contribute cash, whereas others contributed artistic talents, services, etc.

It is true that in some instances the partners created corporations which the partnership owned, con-

trolled and operated for the purpose of advancing its film activities. All corporate expenses were paid by the partnership, and the partners acted in respect to the corporation only to promote the partnership business.

See *Giblin v. Commissioner* (1955), 227 F. 2d 692 (C.C.A. 5), which held that the taxpayer was entitled to a business bad debt deduction in connection with a loan to a company he had promoted, stating:

“Petitioner’s right to deduct the amount of the cancelled debt depends not upon his showing, as the Tax Court seemed to think, that he was in the business of lending money, but rather that he was regularly engaged in the business of ‘dealing in enterprises,’ during the course of which he operated either as a proprietor, as a stockholder, as a partner or as a lender or in a combination of these capacities, contributing to each enterprise his own initiative and energy, and such financial backing as it required.”

In that case the Court also held as time and effort spent on taxpayer’s business, the time he spent on the affairs of the corporation he formed, as this activity was part of his individual business.

Appellee argued to the jury and now in its brief that acts in connection with the corporations formed by the partnership cannot be regarded as activities of the partnership. Although we do not suggest that every act of a corporation thus formed is the act of the partnership, we urge that every act of a partner of H. Koch & Sons in furthering the business of these corporations was a business act of the partnership. The

partnership activated corporations in order to have a vehicle to finance and through which the partnership's funds could be utilized for such financing.

In *Commissioner of Internal Revenue v. Stokes' Estate*, (1953), 200 F. 2d 637 (C.C.A. 3), the Court held that the taxpayer was engaged individually in the business of exploiting patents even though the activities were conducted through corporations activated by him. The Court specifically considered *Dalton v. Bowers* (1932), 287 U.S. 404; *Burnet v. Clark* (1932), 287 U.S. 410; *Higgins v. Commissioner* (1941), 312 U.S. 212, and other cases cited by appellee and distinguished the same. The Court held:

“That the evidence established that his activities in locating, developing and exploiting patents involved much more than the mere investment of funds in and management of corporations.”

*Foss v. Commissioner* (1935), 75 F. 2d 326 (C.C. A. 1) and *Kales v. Commissioner* (1939), 101 F. 2d 35 (C.C.A. 6), which hold to the same effect, are cited with approval by this Honorable Court in *Maloney v. Spencer* (1949), 172 F. 2d 638 (C.C.A. 9); and this Honorable Court in that case distinguished substantially the authorities cited by appellee and held that the taxpayer was engaged “in the business of acquiring, owning, expanding, equipping and leasing food processing plants”.



## II.

**THE PARTNERSHIP AGREEMENT WAS MISINTERPRETED AND THE ENTIRE PRESENTATION AND CONSIDERATION OF THE CAUSE WAS PREJUDICED THEREBY.**

The cause was essentially tried and determined by the trial Court. The trial Court made its findings of fact, and conclusions of law, and granted judgment. The parties could only agree upon one interrogatory to be propounded to the jury and therefore, by stipulation, all other matters were left for determination by the trial Court (R. 293).

The interrogatory was: "During the year 1947, was H. Koch & Sons regularly engaged in the financing of motion picture ventures?" The answer to this interrogatory required (a) proper interpretation of the partnership agreement; and (b) determination as to whether or not the transaction from which the loss resulted was an isolated transaction as distinguished from a course of business. In this latter respect it became essential to consider each and all of the activities of the partnership to establish the time and effort expended and continuity of activity.

(a) The trial Court misinterpreted the partnership agreement (Appellants' Brief, Appendix B, page x) and thereby prevented fair and appropriate consideration of the facts.

The agreement provided:

"... engage in the business of financing motion picture productions . . . if any individual partner or partners desires to advance any sums toward the above mentioned business activity over

and above the sum advanced by this partnership that the profits realized on such sums advanced by the individual partners or the partnership shall be divided as follows: . . . The profit on such sum or sums advanced by any one or more partners over and above that advanced by the other partner or partners shall belong to the individual partner or partners so advancing any excess; . . . The losses on any sums advanced by individual partners over and above that advanced by the other partner or partners equally shall be borne wholly by said partner or partners so advancing such excess. . . . Maurice P. Koch is hereby appointed General Manager of that portion of the partnership business . . . and any expenses . . . shall be borne by the said partnership . . . as such General Manager the said Maurice P. Koch is hereby authorized to deal in his own name. . . .”

The pleadings admit that the partners advanced a total of \$90,000.00 and that complete loss resulted. The entire sum was drawn from partnership funds; however, after the advancements were made, the partnership was short of cash and Maurice P. Koch borrowed and advanced to the partnership \$15,000.00 to replace some of the funds advanced (R. 287). Therefore, under the partnership agreement Maurice P. Koch suffered the loss of \$15,000.00 more than his co-partners. The trial Court refused to understand that even though additional funds were advanced by one of the partners, such advances were nevertheless partnership activities and are governed by the part-

nership agreement. By reason of this misinterpretation the trial Court ruled that in order to establish the additional \$15,000.00 loss, Maurice Koch had to be individually engaged in the business (as distinguished from the partnership). Admittedly all of his acts were on behalf of the partnership and he was not at any time individually engaged in motion picture ventures. Therefore, without hearing argument, and contrary to the admissions of the pleadings, the Court granted dismissal (or directed verdict) against Maurice P. Koch (and his wife) with regard to the added \$15,000.00 loss (R. 292) and the Court made its finding (Finding No. 6, R. 8) that only \$75,000.00 was lost, in the face of pleadings which admit that \$90,000.00 was lost.

(b) Perhaps more devastating was the Court's instruction to the jury to disregard all the activities of Maurice P. Koch in his own behalf. Pursuant to the partnership agreement he managed and conducted all of the partnership affairs in connection with films and all documentation was in his name. Each and all of his activities were for the partnership and only for the partnership (R. 43, 44, 45, 56, 57, 72, 76, 96, 97, 101, 112, 122-125). By ruling that Maurice Koch could not assert the \$15,000.00 loss because he was not individually engaged in the business, the trial Court ruled as a matter of law that he had absolutely no activities in motion picture ventures on his own behalf. Nevertheless the Court instructed the jury that it could not consider Maurice Koch's activities on his own behalf in determining whether or not the partner-

ship was engaged in the business (R. 302). Exception was taken (R. 311-312). There is absolutely no theory of fact in the entire case on which such an instruction could have been predicated. The suggestion thus made that he was engaged on his own behalf was prejudicial. By the terms of the formal partnership agreement Maurice Koch was the Manager of the partnership; managed and conducted all of the picture activities; and was authorized to act in his own name. Under the instruction the jury was prone to disregard all documentation bearing his name, and all activities conducted by him, despite the fact that the same were partnership activities and paid for by the partnership in every respect. This prejudicial error was then compounded by the Government argument to the effect that his activities must be disregarded (R. 349, 352-354). Having captured a directed verdict or dismissal on the Court's own motion, the Government then proceeded to advise the jury that Maurice Koch's activities were in his own behalf and not for the partnership and that his activities should not be considered. Since he conducted all of the activities of the partnership, the prejudice is evident.

Regardless of what action the jury may have taken, the Court's findings on the subject are in error. The pleadings admit the loss of \$90,000.00, not \$75,000.00 as found by the Court (Finding 6; R. 8). The Court failed to make a finding that all of Maurice Koch's activities were on behalf of the partnership, though the Court ruled, as a matter of law, that all of his activities were on behalf of the partnership. On the other

hand, the Court made a finding that Maurice Koch was not individually engaged in the business despite the fact that there was no issue thereon (Finding 10; R. 10). These findings merely emphasize the Court's erroneous interpretation of the partnership contract and the issues in the cause. The entire cause was tried and determined upon these false premises.

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### III.

#### CORRECTION OF FACTS.

Space does not permit complete correction of appellee's statements of facts; however, we note particularly the following:

(1) Appellee's statement regarding the \$15,000.00 advanced to David Sebastian is incorrect. This sum was advanced to organize and activate Beacon Pictures Corporation for the production of the picture "Copacabana". The check for this amount was received in evidence as Exhibit 6 (R. 47). The check was drawn by the partnership on partnership funds and had no particular connection whatsoever with the \$15,000.00 additional loss suffered by Maurice Koch by reason of an equal sum contributed by him to the partnership some seven months later. The stock of the corporation had to be held (pursuant to Exhibit 5 for identification) (Appellants' Brief, Appendix D, page xvi) in the name of Koslow, although by said agreement, which the Court erroneously rejected, the corporation could then assign proceeds and profits received from the picture to others. The pleadings

admitted the loss of all funds alleged to have been lost and there is no issue regarding same. In any event, it was clear that these funds would only be repaid in the event the picture was successful and proceeds were received (R. 250-252). Admittedly the sums were lost; there is no issue thereon; and the argument has no bearing on this case.

(2) Ambassador Productions, Inc. was also formed in order to "package a deal" to finance. The shares were issued in the name of Maurice P. Koch pursuant to the partnership agreement which authorized all transactions to be conducted in his name. The mere existence of the corporation does not negative the partnership activities in regard to the corporation as well as by means of the corporation.

(3) Producers Finance Corporation was also formed and conducted by the partnership, at partnership expense. The purpose was likewise to create a situation which required financing and to also provide a means for raising funds from others.

(4) Admittedly Maurice P. Koch and the various attorneys for the partnership were officers and directors of the various corporations which were formed and activated; however, this was done to promote partnership purposes. The argument by appellee to the jury and in its brief that when Mr. Koch or the attorneys become directors or officers of the corporation, their acts are no longer acts of the partnership is untenable.

(5) Appellee's Statement of The Case lists only a few activities and omits the fact that during the exact

time in question appellants conducted many other film financing matters as disclosed by the record (R. 62, 63, 67, 68, 75, 76, 77, 78, 80, 81, 82, 83, 84, 85, 86, 87, 89, 90, 91, 92, 93, 94, 95, 97, 98, 99, 100, 104, 106, 107, 108, 110, 111, 112, 113, 114, 122, 123, 124, 125, 126, 127, 128, 129, 130, 132, 134, 159, 161, 165, 166, 173, 174, 176, 183, 184, 191, 192, 193, 194, 198, 199, 201, 202, 208, 209, 210, 213, 214, 215, 216, 218, 220, 221, 231, 234, 235, 236, 237, 238, 239, 240, 241, 242, 243, 244, 247).

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#### IV.

#### **RE THE PRESUMPTION OF CORRECTNESS OF DETERMINATIONS BY THE COMMISSIONER OF INTERNAL REVENUE.**

(a) The Government had no witnesses and, in fact, offered no testimony which could in any manner affect the determination of the cause. The Government's defense was based entirely upon the alleged presumption of correctness of the determination by the Commissioner of Internal Revenue. Meticulous examination of the record reveals absolutely no materials, testimony or evidence upon which a defense could be predicated in the absence of such alleged presumption.

(b) The effect of the presumption was discussed with the trial Court and the Court made its position quite clear upon the subject during the trial and before arguments and instructions.

(c) This was, in fact, a trial by the Court and not by the jury whose function was limited to a single interrogatory. The erroneous ruling with regard to

this presumption of correctness of the Commissioner's determination was the basis for the trial Court's findings of fact, as well as conclusions of law.

(d) The Court ruled clearly during the trial, during argument, during instructions, in its findings of fact, in its conclusions of law, and in its judgment that there was a presumption that the determination by the Commissioner of Internal Revenue that the plaintiffs were not engaged in the trade or business of financing motion pictures was correct; and that the burden was upon plaintiff to overcome the presumption of the correctness of the Commissioner's determination by *a preponderance of the evidence* (R. 9, 301, 344). Unfortunately, considerations of the subject off the record do not appear.

(e) For the reason that it constituted the only defense of the Government, the matter of the presumption and overcoming the same became the *central issue in the case*.

(f) Contrary to the rule repeatedly announced by this Honorable Court holding that after evidence is introduced "the Commissioner's determination is no longer existent" . . . "The issue depended wholly upon the evidence" . . . "Find from the evidence and from it alone" . . .<sup>1</sup>, the trial Court consistently enforced its

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<sup>1</sup>The words are excerpts from the Ninth Circuit cases as follows:

*San Joaquin Brick Co. v. Commissioner of Internal Revenue* (1942), 130 F. 2d 220, 225;

*Hemphill Schools v. Commissioner of Internal Revenue* (1943), 137 F. 2d 961, 964;

*Lawrence v. Commissioner of Internal Revenue* (1944), 143 F. 2d 456.



erroneous rule that the presumption survived all evidence in the case. Thus the presentation of the cause was necessarily required to conform to the law of the case as determined by the trial Court and as counsel knew the Court would instruct the jury, and upon which the parties knew the Court would premise its findings and conclusions. Under this erroneous concept, a *prima facie* case could not survive because it was here necessary to overcome the presumption by a preponderance of evidence.

(g) As stated in *Harlem Taxicab Association v. Nemesh* (1951), 191 F. 2d 459, 461, where the Court considered erroneous instructions regarding the effect of a presumption and to which no exception had been taken:

“But the court had repeatedly stated its view of the law in the course of the trial and had repeatedly prevented appellant’s counsel from proceeding on the opposite view. ‘The purpose of exceptions is to inform the trial judge of possible errors so that he may have an opportunity to reconsider his rulings and if necessary correct them.’ It would have been only a formality to ask the court at the end of the trial to reverse itself. An error in instructing a jury may be raised by an appellate court, when justice seems to require, even though it cannot be raised by the appellant.”

After the cause had been tried on the erroneous theory of law, and after the trial Court had specifically considered the proposition of law, and after argument by counsel framed in accordance with the trial Court’s

view of the law, and after the erroneous instructions by the Court in accordance with the erroneous rulings,—the formality of requesting the Court to make corrections in its instructions to the jury would have been nugatory and a sham. Only a new and different trial could obviate the error.

(h) In *Hormel v. Helvering* (1941), 312 U.S. 552, 557, 61 S.Ct. 719, 85 L.Ed. 1037, the Supreme Court stated:

“Rules of practice and procedure are devised to promote the ends of justice, not to defeat them. A rigid and undeviating judicially declared practice under which courts of review would invariably and under all circumstances decline to consider all questions which had not previously been specifically urged would be out of harmony with this policy. Orderly rules of procedure do not require sacrifice of the rules of fundamental justice.”

(i) See appellee’s argument to the jury re “plaintiffs already had one crack at this case” (R. 344 and the Government’s final emotional appeal to the jury: “we submit to you, ladies and gentlemen, the finding of the Commissioner of Internal Revenue, who was duly and legally appointed executive officer of the Government, sworn to administer internal revenue laws, . . .” (R. 370-371)).

We submit, without painstaking or apology, that the Government’s entire argument to the jury was shocking in the extreme. The same did not adhere to the known law of the case; was based upon misstatement

of law and fact, and the officer of the people and whom the jury therefore received as their own adviser, effectively and passionately injected mistrust, contrivance, unwarranted personal attacks, and in finality rested upon the "duly and legally appointed and executive officer of the Government sworn to administer revenue laws . . .", to wit: the determination of the Commissioner of Internal Revenue, as the basis for the jury's finding.

(j) Even though Fed. R. Civ. P. 51 may apply to the special type of trial had in this cause, this Honorable Court nevertheless has the inherent power to note "plain error" related to the central issue in the cause in order to prevent manifest injustice.

We note that all of the Circuits (with the possible exception of the Ninth Circuit), to the extent that the question has arisen, have held that Appellate Courts may apply the doctrine of "plain error". See *Giacalone v. Raytheon Manufacturing Co.* (1955), 222 F. 2d 249 (C.C.A. 1), where the Court stated:

"It does not follow from this, however, that under no circumstances can we consider the error on our own volition."

The Second Circuit recognizes the rule in the following cases:

*Moore v. Waring* (1952), 200 F. 2d 491;

*Finn v. Wood* (1950), 178 F. 2d 583.

The Fourth Circuit considers the matter in *Hite v. Western Maryland Railway* (1954), 217 F. 2d 781, 782:

“If there had been error in the instruction to the jury which in our opinion had led to a miscarriage of justice, we might notice it under our power to notice plain error not assigned to prevent injustice, but there was no such error.”

The Fifth Circuit stated in *Louisiana & Arkansas Railway Company v. Moore* (1956), 229 F. 2d 1:

“However, since it goes to the central issue in the case . . . we may consider it under the general rule which allows an appellate court to notice plain errors, although they were not properly excepted to below.”

To the same effect, see *United States v. Chemell* (1957), 243 F. 2d 944 (C.C.A. 5).

The Eighth Circuit recognizes the rule in *O'Malley v. Cover* (1955), 221 F. 2d 156.

The Tenth Circuit also recognizes the rule in *Allen v. Nelson Dodd Produce Co.* (1953), 207 F. 2d 296, 297.

The Court of Appeals for the District of Columbia enunciated the rule in *Harlem Taxicab Association v. Nemesh, supra*. This Court has enacted its own rule for that District, enunciating that that Court will notice and pass upon “plain error”, and has exercised this power in situations where there is failure to comply with said Rule 51. By adopting its own rule relating to “plain error”, that Court has held that Rule 51 does not eliminate the inherent power of the Court to pass upon matters of “plain error” to prevent injustice. See also *Montgomery v. Virginia Stage Lines* (1951), 191 F. 2d 770 (C.C.A.D.C.).

For comparison, see also *Hormel v. Helvering, supra*.

This Honorable Court gave consideration to the matter of "plain error" in *Walker v. West Coast Fast Freight, Inc.* (1956), 233 F. 2d 939 (C.C.A. 9), and in *Flintkote Company v. Lysfjord* (1957), 246 F. 2d 368 (C.C.A. 9).

Since rules of procedure should not require sacrifice of the rules of fundamental justice, we fervently trust that this Honorable Court will announce the rule of "plain error" in accordance with the holding of all other Courts which have passed upon the matter. However, in this cause the trial Court made its own findings and conclusions based upon the view that the presumption persisted and had more probative value than the evidence offered, and the trial Court granted the judgment. The trial Court likewise permitted argument to the jury, over appellants' objection, upon this same erroneous theory. It is, therefore, not necessary to invoke the doctrine of "plain error" in order to reverse the trial Court.

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## V.

### APPELLANTS WERE ENGAGED IN A TRADE OR BUSINESS WITHIN THE MEANING OF THE INTERNAL REVENUE LAW.

Four persons *agreed by formal agreement*, executed some years prior to the loss in question to enter into a business and did, in fact, enter into the business and pursue the same over a course of years. All of the cases on the subject which have gone into the details

of activities are, in fact, merely probing the intention of an individual who may or may not have formed the intent to conduct particular operations as a business. Never before has the question been raised in a situation where two or more persons have agreed to enter into a particular business and have actually pursued the same. The final issue is a matter of intent, e.g., a builder may be in the building business although he never completes his first structure; a lawyer is in such business even though he never gets a case. The only reason why the Courts permit the probing of activities is to establish the intent by the overt acts. In the present cause, the intent of the four partners was established by their written contract and acts thereunder years prior to the time in question. We submit that there is no case in which two or more people have agreed by written agreement to engage in a certain business which has previously been challenged by the Government. We submit that there is no basis for such challenge and the parties to the agreement are entitled to recognition of the terms thereof. The Government cannot tell taxpayers that they may not engage in a particular business in accordance with their formal agreement.

If a profit had resulted from the sale of an interest acquired, the Government would not permit capital gain treatment. The Commissioner would take the obvious position that by their own agreements appellants were "in the business" of financing picture ventures and as such are not entitled to capital gain treatment. On the other hand, the Government now argues that the loss is a capital loss despite the fact

that by their solemn agreement and conduct appellants engaged in the business and could not realize a capital gain.

Appellee admits that one may be in the business of making loans and that one who merely made a number of loans to film companies would be in a business recognized for tax purposes. On the other hand, appellee argues that one who expends money, time and effort to locate artistic elements, and to set up production vehicles, and who raises funds and utilizes the same in the preproduction costs in connection with films, is not engaged in a business recognized for tax purposes, no matter how much money, time and effort is expended in this activity. The argument is untenable.

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## VI.

### CONCLUSION.

We respectfully submit that the cause should be remanded to the trial Court for the computation of the amounts due appellants. In the alternative, we submit that the judgment should be reversed and the cause remanded for trial.

Dated, San Francisco, California,  
June 2, 1958.

Respectfully submitted,

MAX FINK,

LEON SCHILLER,

*Attorneys for Appellants.*





No. 15646

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**United States  
Court of Appeals**

**For the Ninth Circuit**

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**OTTO W. HEIDER,**

**Appellant.**

**vs.**

**SAMUEL A. McALLISTER, Trustee in Bank-  
ruptcy of the Estate of Rand Truck Line, Inc.,**

**Appellee.**

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**Transcript of Record**  
**FILED**

**DEC 20 1957**

**PAUL P. GIBBENT, CLERK**

**Appeal from the United States District Court for the  
District of Oregon**



No. 15646

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**United States  
Court of Appeals**  
*For the Ninth Circuit*

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**OTTO W. HEIDER,**

**Appellant.**

**vs.**

**SAMUEL A. McALLISTER, Trustee in Bank-  
ruptcy of the Estate of Rand Truck Line, Inc.,**

**Appellee.**

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**Transcript of Record**

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1. The first part of the report is a general  
introduction to the subject of the study.  
2. The second part is a description of the  
methodology used in the study.  
3. The third part is a description of the  
results of the study.  
4. The fourth part is a discussion of the  
results of the study.  
5. The fifth part is a conclusion of the  
study.  
6. The sixth part is a list of references.  
7. The seventh part is an appendix.  
8. The eighth part is a list of figures.  
9. The ninth part is a list of tables.  
10. The tenth part is a list of abbreviations.

NAMES ARE

WILLIAM

R. CARR

PHILIP

ROBERT

THOMAS

JOHN

WILLIAM

ROBERT

THOMAS

JOHN

WILLIAM

ROBERT

THOMAS

JOHN

WILLIAM

ROBERT

THOMAS

JOHN

WILLIAM

ROBERT

THOMAS

JOHN

WILLIAM

ROBERT

THOMAS





## NAMES AND ADDRESSES OF ATTORNEYS

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**J. H. CAIRNS,**

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Portland, Oregon,

For Appellant.

**C. X. BOLLENBACK,**

825 Failing Building,

Portland, Oregon, and

**F. BROCK MILLER,**

Pittock Block,

Portland, Oregon,

Attorneys for Appellee.

WILLIAM H. HARRIS, JR.

WILLIAM H. HARRIS, JR.

WILLIAM H. HARRIS, JR.

WILLIAM H. HARRIS, JR.

WILLIAM H. HARRIS, JR.

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WILLIAM H. HARRIS, JR.

WILLIAM H. HARRIS, JR.

WILLIAM H. HARRIS, JR.

District Court of the United States  
For the District of Oregon  
No. B-29990

In the Matter of:

RAND TRUCK LINE, INC., an Oregon Corporation

ORDER OF GENERAL REFERENCE  
IN JUDGE'S ABSENCE

At Portland, in said district, on the 20th day of May, 1949,

Whereas a petition was filed in this court, on the 20th day of May, 1949, by Rand Truck Line, Inc., an Oregon Corporation, the bankrupt above named, praying that it be adjudged a bankrupt under the Act of Congress relating to bankruptcy; and whereas the judges of said court are absent from the City of Portland, and pursuant to a standing order of this court dated June 25, 1942,

It is Ordered that the above-entitled proceeding be, and it hereby is, referred to Estes Snedecor, one of the referees in bankruptcy of this court, to take such further proceedings therein as are required and permitted by said Act.

Witness my hand and the seal of said Court.

[Seal]                      LOWELL MUNDORFF,  
Clerk.

By /s/ E. M. DAVIS,  
Deputy.

[Endorsed]: Filed May 20, 1949.

[Title of District Court and Cause.]

## ADJUDICATION OF BANKRUPTCY

At Portland, in said district, on the 23rd day of May, 1949.

The petition of Rand Truck Line, Inc., filed on the 20th day of May, 1949, that it be adjudged a bankrupt under the act of Congress relating to bankruptcy, having been heard and duly considered.

It is adjudged that the said Rand Truck Line, Inc., an Oregon corporation is a bankrupt under the act of Congress relating to bankruptcy.

/s/ JAMES ALGER FEE,  
District Judge.

[Endorsed]: Filed May 23, 1949.

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[Title of District Court and Cause.]

## ORDER APPROVING TRUSTEE'S BOND

At a session of the Court of Bankruptcy, held in and for said District of Oregon, before Estes Snedecor, Referee in Bankruptcy, at Portland, Oregon, this 8th day of June, 1949.

The above-named Rand Truck Line, Inc., an Oregon corporation, having been duly adjudged a bankrupt on a petition filed by it on the 20th day of May, 1949; and Samuel A. McAllister of Portland in said District, having been duly appointed trustee of the estate of said bankrupt, and having duly qualified by giving a bond with sufficient sureties for

the faithful performance of his official duties in the amount fixed by the order of this court, viz., \$10,000.00; it is

Ordered that the said bond be, and it hereby is, approved.

/s/ ESTES SNEDECOR,  
Referee in Bankruptcy.

[Endorsed]: Filed June 9, 1949.

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[Title of District Court and Cause.]

### PROOF OF SECURED DEBT

At Sheridan, in the County of Yamhill, State of Oregon, on this 23rd day of June, 1949, comes Otto W. Heider of said county and state, and makes oath and says:

(1) That he hereinafter designates himself as claimant.

(2) That said claimant is doing business at the place aforesaid, and that said corporation in whose court proceedings this proof of debt is filed was at and before the aforementioned court proceedings were filed in said court, and still is, justly and truly indebted to said claimant in the sum of \$11,500.00. That the consideration of said debt is as follows: The paying off of prior, present and current obligations, notes, mortgages and liabilities of the Rand Truck Line, outstanding and existing on the 7th day of August, 1946, together with cash disbursements, and which prior evidence of indebtedness having been heretofore returned to the makers thereof.

That no part of the balance of said debt above set forth in the sum of \$11,500.00 has been paid; that there are no offsets or counterclaims against the said sum herein alleged to be due; that deponent has not, nor has any person for and on behalf of said claimant, or to this deponent's knowledge or belief, for claimant's use, had or received any manner of security for the said debt other than as herein stated, nor has any judgment been rendered for any part thereof, nor has any note or other evidence of debt been received except as herein stated and set forth.

Affiant further says said debt herein proven, and this claim are free from usury as defined by the laws of the state of Oregon wherein the debt was contracted.

That the said claimant reserves the right and/or constitutes and appoints ..... to attend any and all creditors' meetings of the aforesaid corporation in said proceedings above styled, for and in the name of the claimant, to vote for or against any proposal or resolution, and accept in writing or fail to accept in writing any proposal of composition or extension that may be submitted under the laws of the United States in said proceedings; to vote for the trustee, to object to confirmation of composition or extension offered in this proceedings; and to receive payment of dividends, distribution of moneys due claimant or which might be paid to claimant under any and all proceedings, and to act in said proceedings to claimant's interest with full power of substitution; and all other powers

of attorney heretofore given in regard to the above styled proceedings are hereby revoked.

That hereto attached and marked Exhibit "A" and made a part hereof as fully and completely as if incorporated herein is a combination real estate and personal property mortgage dated the 7th day of August, 1946, and filed with county clerk of Yamhill County, Oregon, on the 9th day of August, 1946, and recorded in Vol. 107, page 676, Record of Real Estate Mortgages of Yamhill County, Oregon, and was filed in the office of the Secretary of State at Salem, Oregon in the Record of Migratory Chattels, and which mortgage was executed by the Rand Truck Line, an Oregon Corporation, et al., as mortgagor, to H. H. Macy, Vern Markee, Florence Markee and Lorn Markee as mortgagees, and thereafter the said mortgage and promissory note hereto attached and made a part hereof was subsequently and on the 7th day of August, 1946, assigned and transferred for value, without notice and before maturity to the claimant who is now the owner and holder of said mortgage and promissory note herein set forth and described.

That in addition to the foregoing security, and as collateral security for the payment of the obligation herein set forth the following shares and certificates of stock in Rand Truck Line, Inc., were assigned, set over and transferred to the claimant, who is now the owner and holder thereof, and said stock is described as follows, to wit:

Certificate No. 27 for 930 shares, formerly owned by Beryl Taylor, dated April 18, 1949.

Certificate No. 26 for 615 shares, formerly owned by Rand Truck Line, Dated April 18, 1949.

Certificate No. 28 for 920 shares, formerly owned by Lorn E. Markee, dated April 18, 1949.

Certificate No. 25 for 920 shares, formerly owned by Harold H. Macy, dated April 18, 1949.

That the said claimant holds the certificates of title to said vehicles described in said mortgage, and is shown to be the legal owner thereof, and the same are briefly described as follows:

Cert. of Title No.	Year	Kind	Factory No.
A817044	1939	International tk.	8646
C1069501	1939	Chevrolet truck	T2639636 (Motor N
1179766	1935	Wentwin trailer	SP3103
1179543	1940	Trombly trailer	382
1143460	1936	Trailmobile tr.	SP3104
1179542	1926	Wentwin trailer	340
1143452		Utility trailer	59672
A1189570	1946	Transport van	M3L11022
1179767		Trailmobile tr.	17233
1179544	1944	Fruehauf trailer	C8632
748381	1937	International tk.	1552
1179545	1936	Trailmobile	D58507
A887489	1940	Int'l tractor	772
1162014	1945	Fruehauf tr.	C9031
A560350	1934	Int'l tk.	FAB4179 (Motor N
947019	1941	International tk.	1120
863473	1940	International tk.	1865
A667301	1936	International tk.	808
A948417	1941	Dodge tk.	9275402
1143451	1928	Wentwin & Irwin tra.	6290
D804590	1938	International tk.	3500
A842270	1939	International tk.	1203
B687345	1936	Chevrolet tk.	6RD0711149
A1124373	1937	Inter. tract.	DR60553
1014403	1942	Int'l tk.	3138
A1015945	1942	Int'l tk.	3115
C575985	1934	Dodge tk.	9243940



That said mortgage and note is in default in that \$1,000.00 was due on the 1st day of May, 1949, and only \$500.00 was paid on the 10th day of May, 1949, and \$1,000.00 was due on the first day of June, 1949, and no part of said monthly installment has been paid, and by reason of the breach of the terms and conditions of said mortgage the same is all due and claimant declares it all due and payable and the said mortgage is subject to immediate foreclosure, and the said note and mortgage bears interest at the rate of 8% per annum from the maturity of the monthly installments due and not paid.

/s/ OTTO W. HEIDER.

Subscribed and sworn to before me this 23rd day of June, 1949.

/s/ IRENE LAWRENCE,

Notary Public for Oregon,

My com. expires Nov. 9, 1951.

EXHIBIT A

(Original)

Mortgage

(Real and Personal)

Rand Truck Line

To

H. H. Macy, et al.

This Indenture, Made this 7th day of August in the year One Thousand Nine Hundred and forty-six,

between Rand Truck Line, an Oregon Corporation, Vern Markee, Florence Markee, his wife as mortgagors, and H. H. Macy, Vern Markee, Florence Markee and Loren Markee as mortgagee,

Witnesseth, That the said mortgagors for and in consideration of the sum of Forty-three thousand five hundred sixty 00/100 Dollars (\$43,560) to them paid by the said mortgagees, do hereby grant, bargain, sell and convey unto the said mortgagees and assigns those certain premises situated in the County of Yamhill, and State of Oregon, and described as follows:

Lot No. 5 and the North 15 ft. of Lot 6 of Block One of Morgan's Addition to the City of Sheridan, Yamhill County, Oregon, according to the duly recorded map and plat thereof, subject to any dedicated, vacated or conveyed rights heretofore by which there has been legally established an alley, easement or right-of-way for travel from the east end of the above-described property and the lots immediately to the east.

Together with all and singular the tenements, hereditaments and appurtenances thereunto belonging or in anywise appertaining, and which may hereafter thereto belong or appertain, and the rents, issues and profits therefrom, and any and all fixtures upon said premises at the time of the execution of this mortgage or at any time during the term of this mortgage.

To Have and to Hold the said premises with the appurtenances unto the said mortgagee and assigns forever.

This Conveyance is intended as a Mortgage to secure the payment of the sum of Forty-three thousand five hundred sixty and 00/100 Dollars (\$43,560.00) in accordance with the terms of a certain promissory note of which the following is substantially a copy, to wit:

It is understood definitely that the Rand Truck Line and/or mortgagors will do their own insuring as to public liability and property damage, fire, theft and collision at their own expense, and that the legal owner of said equipment and holder of this mortgage is under no obligation in connection therewith.

This mortgage is executed for a present and current consideration to take up present and outstanding obligations of mortgagor, and is not given for any past consideration.

This indenture is further conditioned upon the faithful observance by the mortgagors of the following covenants hereby expressly entered into by the mortgagor, to wit:

That they are lawfully seized of said premises, and now have a valid and unincumbered fee simple title thereto, and that they will forever warrant and defend the same against the claims and demands of all persons whomsoever;

That they will pay the said promissory note and all installments of interest thereon promptly as the same become due, according to the tenor of said note;

That so long as this mortgage shall remain in force they will pay all taxes, assessments, and other charges of every nature which may be levied or assessed upon or against the said premises when due and payable, according to law, and before the same become delinquent, and will also pay all taxes which may be levied or assessed on this mortgage or the debt thereby secured, and will promptly pay and satisfy any mechanic's liens or other incumbrances that might by operation of law or otherwise become a lien upon the mortgaged premises superior to the lien of this mortgage;

That they will keep all the improvements erected on said premises in good order and repair and will not commit or suffer any waste of the premises hereby mortgaged;

That so long as this mortgage shall remain in force they will keep the buildings now erected, or any which may hereafter be erected on said premises, insured against loss or damage by fire to the extent of \$ none in some company or companies acceptable to said mortgagee and for the benefit of said mortgagee, and will deliver all the policies and renewals thereof to said mortgagee.

Now, Therefore, if the said mortgagors shall pay said promissory note, and shall fully satisfy and comply with the covenants hereinbefore set forth, then this conveyance shall be void, but otherwise to remain in full force and virtue as a mortgage to secure the payment of said promissory note in accordance with the terms thereof and the perform-

ance of the covenants and agreements herein contained; it being agreed that any failure to make any of the payments provided for in said note or this mortgage when the same shall become due or payable, or to perform any agreement herein contained, shall give to the mortgagees the option to declare the whole amount due on said note, or unpaid thereon or on this mortgage, at once due and payable and this mortgage by reason thereof may be foreclosed at any time thereafter. And if the said mortgagors shall fail to pay any taxes or other charges or any lien or insurance premium as herein provided to be done, the mortgagees shall have the option to pay the same and any payment so made shall be added to and become a part of the debt secured by this mortgage, and draw interest at the rate of ten per cent per annum, without waiver, however, of any right arising from breach of any of the covenants herein.

In case a complaint is filed in a suit brought to foreclose this mortgage, the court shall, upon motion of the holder of the mortgage, without respect to the condition of the property herein described, appoint a receiver to collect the rents and profits arising out of said premises, and apply such rents and profits to the payment and satisfaction of the amount due under this mortgage, first deducting all proper charges and expenses attending the execution of such trust.

In the event of suit or action being instituted to foreclose this mortgage, the mortgagors and/or their

assigns shall pay such sum as the Court shall consider reasonable, as attorneys' fees for the benefit of the plaintiff, in addition to the costs and disbursements provided by statute.

As to the personal property the following shall apply: But if default shall be made in the payment of said debt, interest charges, or payments or any conditions of said mortgage, according to the terms of the said note or if first parties shall offer for sale, sell, assign, encumber or dispose of all or any part of said goods and chattels, or shall remove or attempt to remove all or any part thereof from the above-described premises without the written consent of the mortgagee or holder of this mortgage, whether said indebtedness shall be then due or not, or if the representations of first parties herein contained are in whole or in part untrue, then and from thenceforth it shall be lawful and the mortgagee, its agents, successors and assigns are hereby authorized to sell all or any part of the said property for cash at private sale or public auction for the best price that it can obtain and first parties waive personal notice thereof, or any other kind of notice, and the mortgagee may buy at such sale and the said property may be so sold in bulk or in parcels, or so much thereof as shall be necessary to satisfy the said debt, interest and charges, plus lawful expenses of sale, and reasonable attorney's fee, if any, and the mortgagee may retain all the said amounts out of the proceeds of said sale, and shall return the overplus, if any, to first parties; for the purpose of enforcing the provisions and conditions

hereof the mortgagee, its agents, successors and assigns are hereby authorized and empowered to enter upon the premises of first parties or any place where said goods and chattels or any part thereof may be found, and take possession thereof and dispose of the same as hereinbefore provided.

If there is only one first party to this instrument, all plural words used herein with reference to first parties shall be construed in the singular. Acceptance by the mortgagee or any holder of this mortgage, of any payment hereon after the same is due, shall not constitute a waiver by such holder of this or any other provision of this mortgage, and time is the essence hereof.

Any deficiency and shortage unpaid sale and seizure of the property herein described the mortgagor or mortgagors shall immediately pay, and do hereby confess judgment for such shortage or unpaid deficiency, and any circuit court in the state of Oregon shall have jurisdiction in the foreclosure of this mortgage; the chattel mortgage portion of this mortgage may be foreclosed by the holder thereof without the intervention of any court being taken, but in a summary manner as herein provided.

In Witness Whereof, the said mortgagors have hereunto set their hands and seals the day and year first above written. By resolution of its board of directors and its stockholders has caused these presents to be executed by its President, Secretary-Treasurer and General Manager, and its corporate seal to be hereunto affixed this 7th day of August, 1946.

[Seal]            RAND TRUCK LINE,  
                    A Corporation,

By /s/ FLORENCE MARKEE,  
          Secy.-Treas., Personally &  
          Individually.

[Seal]            RAND TRUCK LINE,  
                    A Corporation,

By /s/ VERN MARKEE,  
          President.

[Seal]            RAND TRUCK LINE,  
                    A Corporation,

By /s/ H. H. MACY,  
          General Manager.

/s/ LOREN E. MARKEE,

/s/ FLORENCE MARKEE.

#### Acknowledgment

State of Oregon,  
County of Yamhill—ss.

On this 7th day of August, 1946, before me appeared Vern Markee, Florence Markee and H. H. Macy, to me personally known, who being duly sworn, did say that he, the said Vern Markee is the President, and she, the said Florence Markee is the Secretary-Treasurer, and he, the said H. H. Macy is the General Manager of the within named corporation, and that the seal affixed to said instrument is the corporate seal of said corporation, and that the said instrument was signed and sealed in



behalf of said corporation by authority of its Board of Directors, and the said Vern Markee, Florence Markee and H. H. Macy acknowledge said instrument to be the free act and deed of said corporation.

In Testimony Whereof I have hereunto set my hand and affixed my official seal, this, the day and year first in this, my certificate written.

[Seal]      /s/ IRENE LAWRENCE,  
Notary Public in and for Said  
County and State.

My commission expires Nov. 3, 1947.

Sheridan, Oregon, Aug. 7, 1946.

\$43,560.00

For value received I promise to pay to the order of H. H. Macy, Vern Markee, Florence Markee and Loren Markee at McMinnville, Oregon, Forty-three thousand five hundred sixty and 00/100 Dollars in lawful money of the present standard value, with interest thereon in like lawful money at the rate of 8% per annum from maturity until paid, payable in monthly installments of not less than \$1,000.00 in any one payment, together with the full amount of interest due on this note at time of payment of each installment. The first payment to be made on the 1st day of September, 1946, and a like payment on the 1st day of each month thereafter, until the whole sum, principal and interest, has been paid; if any of said installments are not so paid, the whole sum of both principal and interest, to become immedi-

ately due and collectible at the option of the holder of this note. In case suit or action is instituted to collect this note or any portion thereof, I promise to pay such additional sum as the Court may adjudge reasonable as attorneys fees in said suit or action.

[Seal]                      RAND TRUCK LINE,  
                                    A Corporation,

By /s/ FLORENCE MARKEE,  
                                    Secy.-Treas.

[Seal]                      RAND TRUCK LINE,  
                                    A Corporation,

By /s/ VERN MARKEE,  
                                    President.

[Seal]                      RAND TRUCK LINE,  
                                    A Corporation,

By /s/ H. H. MACY,  
                                    General Manager.

/s/ LOREN E. MARKEE.

Assignment & Guarantee

Sheridan, Ore., Aug. 7, 1946.

For value received I hereby guarantee the payment of the within note, consent to any extension of time granted the maker, and waive protest, demand and notice of non-payment thereof, and in case suit or action is instituted upon this guaranty for the collection of the within note, I promise to pay such

sum as the Court may adjudge reasonable as attorney's fees in such suit or action, all to the same extent as if I were a maker hereof.

/s/ VERN MARKEE,

/s/ FLORENCE MARKEE,

/s/ H. H. MACY,

/s/ LOREN E. MARKEE.

State of Oregon,  
County of Yamhill—ss.

On this the 7th day of Aug., A.D. 1946, personally came before me a Notary Public in and for said County and State, the within-named Loren E. Markee, and Florence Markee, his wife, to me personally known to be the identical persons who executed the within instrument, and acknowledged to me that they executed the same freely for the uses and purposes therein named.

In Testimony Whereof, I have hereunto subscribed my name and affixed my Notarial seal, the day and year last above written.

[Seal]      /s/ IRENE LAWRENCE,  
Notary Public in and for the  
State of Oregon.

My Commission Expires Nov. 3rd, 1947.

[Endorsed]: Filed June 30, 1949, Referee.

[Endorsed]: Filed October 23, 1956, U.S.D.C.

[Title of District Court and Cause.]

OBJECTIONS TO PROOF OF DEBT  
OF OTTO W. HEIDER

To: The Honorable Estes Snedecor, Referee in  
Bankruptcy:

I, Samuel A. McAllister, Trustee in Bankruptcy,  
do hereby object to the Proof of Debt filed herein  
by Otto W. Heider, an alleged secured creditor of  
the bankrupt herein, for the sum of \$11,500.00, upon  
the following grounds and reasons:

As My First Objection Thereto:

I.

I deny each and every allegation, thing and mat-  
ter contained in said Proof of Debt and the whole  
thereof, except as hereinafter specifically set out and  
admitted.

As My Second Objection Thereto, I allege:

I.

That said purported debt is the claimed balance  
upon a purported mortgage claimed to have been  
executed by the bankrupt herein under the follow-  
ing circumstances and conditions:

1. That on or about the 28th day of September,  
1944, and at a time when the assets of said bank-  
rupt did not exceed its liabilities and at a time when  
said bankrupt was operating at a net loss, Vern  
Markee, Florence Markee and Loren Markee pur-

chased 4,000 shares of the capital stock of the Rand Truck Line, Inc., from Robert R. Rand and Mrs. R. R. Rand, also known as Golda I. Rand; that Otto Heider loaned and advanced to the said Vern Markee, Loren Markee and Florence Markee, and paid to the said Robert R. Rand and Mrs. R. R. Rand, also known as Golda I. Rand, for and on their behalf to aid and assist them to purchase said stock, the sum of \$31,500.00; that the said Vern Markee, Florence Markee and Loren Markee attempted to bind and obligate the said Rand Truck Line, Inc., a corporation, to the payment of such personal obligations, namely, payment to Otto Heider of the moneys advanced by the said Otto Heider to the said Vern Markee, Florence Markee and Loren Markee individually for the purchase of said capital stock by causing the said bankrupt, acting through the said Vern Markee, Florence Markee and Loren Markee, to execute a purported note and mortgage in the face amount of \$43,560.00 including interest, in favor of Mrs. R. R. Rand, also known as Golda I. Rand, which said note and mortgage was immediately and as a part of the same transaction delivered to the said Otto Heider.

2. That between September 28, 1944, and until August 7, 1946, the officers, directors and stockholders of said bankrupt diverted and caused to be diverted to their own use and benefit and paid and caused to be paid to the said Otto Heider upon said purported note and mortgage large sums of money belonging to and owned by the bankrupt herein,

namely, approximately \$1,000.00 per month during said period; that on and at a time when there remained a purported balance of \$13,168.00 upon said alleged note and mortgage, a second and subsequent purported note and mortgage was executed by said parties, purporting to bind the bankrupt herein to pay said balance in addition to other moneys then advanced by the said Otto Heider on behalf of the said bankrupt; that thereafter said Vern Markee, Florence Markee, Loren Markee and other agents of said bankrupt continued to divert and cause to be diverted and paid to the said Otto Heider upon said purported second note and mortgage additional large sums of money belonging to and owned by said bankrupt, namely, approximately \$1,000.00 per month until the month of May, 1949; that as the result of such payment so made and so received by the said Otto Heider, more than \$40,000.00 of moneys owned by the said bankrupt were diverted from said corporation and the creditors of said corporation and applied upon the aforesaid individual debts and obligations of the stockholders of the bankrupt herein; that the said Otto Heider, with full knowledge that such sums of money belonged to and were assets of said bankrupt corporation, received and accepted the same and attempted to apply the same in payment of said personal obligations of the said stockholders. That no part of said sums have been repaid to the said bankrupt or to your trustee.

3. That during said period of time, namely, between September 28, 1944, and May 20, 1949, the

said bankrupt did not earn any profits, in excess of operating costs, and did not have nor acquire any surplus funds; that the debts and liabilities of the said bankrupt increased and continued to increase during said period, and remained unpaid to and including the date of adjudication in bankruptcy herein; that the moneys paid out and received as hereinabove alleged were not paid out of net profits or surplus; that the execution of said purported notes and mortgages and payment of the moneys paid out and received as aforesaid rendered and caused the bankrupt herein to become and be insolvent and bankrupt, and unable to pay its debts in the ordinary course of business, and with liabilities exceeding in amount the value of its assets, taken at a fair valuation and exclusive of such moneys so paid and received as herein alleged. That at the time of its adjudication in bankruptcy herein the said Rand Truck Line, Inc., was indebted to various firms and persons and corporations in a total approximate amount of \$40,000.00. That the execution of said purported notes and mortgages and the payments of money paid out and received as hereinabove alleged, hindered, delayed and defrauded creditors of the bankrupt herein, and were intended to and did deprive said creditors of the assets of said corporation and were intended to and did attempt to discharge the aforesaid personal obligations of the stockholders of the bankrupt herein to Otto Heider, to the detriment and damage of such creditors of said corporation.

4. That the said Rand Truck Line, Inc., received nothing of value nor any consideration whatsoever in return for the execution of the first note and mortgage or payment of such personal obligations of the stockholders; that the Articles of Incorporation of the said bankrupt give or grant to said corporation no power to pledge its credit or borrow money for or on behalf of its stockholders, directors, or any other persons whatsoever, or to purchase its own stock for and on behalf of itself or any other person; that the purported execution of the said alleged notes and mortgages, and the payment of said sums, as hereinabove alleged to the said Otto Heider, was and is beyond the power and authority of said corporation, its officers or directors.

And for My Third Objection to Said Alleged Proof of Debt, I allege:

I.

That on or about the 28th day of September, 1944, the said Otto Heider advanced for the use and benefit of the stockholders of the bankrupt herein the sum of \$36,500.00, and the said stockholders attempted to bind the bankrupt herein to repay the sum of \$43,560.00 in payment therefor, and caused said bankrupt to execute a note and mortgage purportedly agreeing to repay said sum of \$43,560.00; that included in the amount of said purported note and mortgage in addition to the alleged principal sum was the sum of \$7,060.00 as prepaid interest; that said prepaid interest was computed and in-



cluded at a rate and in amounts in excess of 10% per annum, namely, at a rate of approximately 10.40% per annum.

## II.

That subsequently thereto and after payments had been made by said bankrupt in the amount of \$30,392.00 upon said purported note and mortgage, with a claimed balance due thereon of \$13,168.00, or \$6,108.00 excluding said item of purported prepaid interest, in consideration of claimed advances of \$22,529.00 to the bankrupt, the stockholders of said bankrupt herein caused the said bankrupt to execute a purported note and mortgage in the amount of \$43,560.00, which note and mortgage purported to include the alleged balance upon said first note and mortgage of \$13,168.00, such claimed advances of \$22,529.00 and prepaid interest in the amount of \$7,533.00. That said prepaid interest was computed and included at a rate and in amounts in excess of 10% per annum, namely, at a rate of approximately 11.275% per annum if the prepaid interest item of said first purported note and mortgage is included in the alleged principal amount or approximately 28.1% if the prepaid interest item of said first purported note and mortgage is excluded therefrom.

## III.

That the purported agreements of the bankrupt to pay said sums representing prepaid interest were demanded and received by the aforesaid Otto Heider as the purported consideration for the alleged extension of time evidenced by said purported

notes and mortgages for the payment of said alleged debts and were included and added to the balances claimed to be due from the bankrupt to Otto Heider knowingly and with the intent on the part of the said Otto Heider to collect and receive and to have the said bankrupt pay interest on such claimed indebtednesses at a rate in excess of 10% per annum.

#### IV.

That the said Otto Heider received and accepted said purported notes and mortgages with full knowledge of the facts herein alleged.

#### V.

That funds of the bankrupt in excess of \$59,029.00 were paid to the said Otto Heider, and any purported balance claimed to be due to the said Otto Heider on said purported notes and mortgages were and are balances representing usurious interest charges computed at a rate in excess of 10% per annum, as hereinabove set out.

Wherefore, your trustee prays for an Order of this Court sustaining his objections, and all of them, to the said claim filed herein by the said Otto Heider, and for such other Orders as to this Court seem just and equitable.

/s/ SAMUEL A. McALLISTER,  
Trustee.

Duly verified.

[Title of District Court and Cause.]

NOTICE OF TIME SET FOR HEARING OF  
OBJECTIONS TO PROOF OF DEBT OTTO  
W. HEIDER

To: Otto W. Heider, Sheridan, Oregon:

You Are Herewith Notified that the hearing upon the objections to Proof of Debt filed by you in the above-entitled proceedings has been set for hearing before the Honorable Estes Snedecor, Referee in Bankruptcy, in Room 521, United States Court House, Portland, Oregon, on the 28th day of February, 1956, at the hour of 2:00 o'clock p.m.

Dated this 26th day of January, 1956.

/s/ C. X. BOLLENBACK,  
Attorney for Trustee.

Affidavit of service by mail attached.

[Endorsed]: Filed January 31, 1956.

[Endorsed]: Filed October 23, 1956, U.S.D.C.

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[Title of District Court and Cause.]

SUPPLEMENTAL OBJECTIONS TO CLAIM  
OF OTTO HEIDER

Comes now Samuel A. McAllister, Trustee and for his fourth objection to said Proof of Claim alleges as follows:

That said claimant is in effect asking this Court to foreclose upon his alleged mortgage, and the facts

and circumstances surrounding execution of said mortgage and the subsequent dealings between said claimant and the mortgagors are a violation of the "clean hands" doctrine and in fact are as follows:

1. That said loan on the part of said claimant was made to Verne Markee, Florence Markee and Loren Markee as a personal loan, but with the knowledge and consent of said claimant, the mortgage was executed to give the appearance of a corporate indebtedness and mortgage.

2. That the interest rate provided for by said claimant is usurious.

3. That said claimant accepted payments upon said mortgage which were in fact diversion of corporation assets with full knowledge that such assets were being diverted.

Wherefore Trustee renews his prayer that the claim of lien and claim of said Otto Heider be disallowed in its entirety.

/s/ SAMUEL A. McALLISTER.

State of Oregon,  
County of Multnomah—ss.

I, Samuel A. McAllister, being first duly sworn, depose and say:

That I am the trustee of the above-entitled estate in bankruptcy; that I have read the within and

foregoing petition, know the contents thereof, and the same are true as I verily believe.

/s/ SAMUEL A. McALLISTER.

Subscribed and sworn to before me this 14th day of March, 1956.

[Seal]      /s/ F. BROCK MILLER,  
Notary Public for Oregon.  
My Commission Expires: November 3, 1957.

[Endorsed]: Filed March 14, 1956, Referee.

[Endorsed]: Filed October 23, 1956, U.S.D.C.

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[Title of District Court and Cause.]

### MOTION TO DISMISS

To: The Honorable Estes Snedecor, Referee in Bankruptcy:

Otto W. Heider, a creditor of the bankrupt herein, moves the Court to dismiss the objections to proof of debt of Otto W. Heider on the ground that the Bankruptcy Court is without jurisdiction to entertain these objections because the same matter has been submitted to the Circuit Court for the State of Oregon, for the County of Multnomah, in the case of Samuel A. McAllister, Trustee in Bankruptcy for Rand Truck Line, Inc., a bankrupt, vs. Vern Markee, Florence Markee, his wife, Loren Markee, Harold Macy, Beryl B. Taylor and Otto Heider, Docket No. 190-145, by authority of the

Honorable Estes W. Snedecor, Referee in Bankruptcy.

/s/ WILLIAM E. DOUGHERTY,  
Of Attorneys for Creditor.

[Endorsed]: Filed March 14, 1956, Referee.

[Endorsed]: Filed October 23, 1956, U.S.D.C.

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[Title of District Court and Cause.]

FINDINGS OF FACT AND  
CONCLUSIONS OF LAW

(Claim of Otto W. Heider and  
Objections of Trustee thereto)

This matter having come on for hearing upon the 14th day of March, 1956, upon the claim of Otto W. Heider filed herein and the Objections of the Trustee thereto, the Trustee appearing personally and by and through his attorneys, C. X. Bollenback and F. Brock Miller, and Otto W. Heider, the Claimant herein, appearing personally and by and through his attorney, William E. Dougherty, evidence having been adduced upon the respective parties and the Court having considered the matter and being fully advised in the premises, make the following:

Findings of Facts

I.

That on or about the 28th day of September, 1944, Vern Markee, Florence Markee and Loren Markee

purchased 4,000 shares of the capital stock of the said Bankrupt from Robert R. Rand, Mrs. Robert R. Rand and a Mrs. Potts; that Otto W. Heider loaned and advanced to the said Vern Markee, Loren Markee and Florence Markee and paid to the said Robert R. Rand, Mrs. Robert R. Rand and Mrs. Potts, for and on behalf of Vern Markee, Loren Markee and Florence Markee, to aid and assist the said Markees to purchase said stock the sum of Thirty-Two Thousand Dollars (\$32,000); that the said Vern Markee, Loren Markee and Florence Markee attempted to bind and obligate the Bankrupt herein, Rand Truck Line, Inc., a corporation, to the payment of such personal obligation, namely, payment to Otto W. Heider of the monies advanced by the said Otto W. Heider to the said Markees individually for the purchase of such said capital stock by causing the said Bankrupt herein, acting through the said Markees, to execute a note and mortgage in the face amount, including prepaid interest, \$43,560, in favor of Mrs. Robert R. Rand, also known as Goldie I. Rand, which said note and mortgage was immediately and as a part of the same transaction assigned and delivered to the said Otto W. Heider.

## II.

That between September 20th, 1944, and August 7th, 1946, the officers, directors and stockholders of the said Bankrupt diverted and caused to be diverted to their own use and benefit and paid and caused to be paid to the said Otto W. Heider, upon said note and mortgage, large sums of money be-

longing to and owned by the Bankrupt herein, namely, Twenty-Four Thousand Five Hundred and No/100 Dollars (\$24,500): that on or about August 7, 1946, and at a time when there remained a balance of Thirteen Thousand One Hundred and Sixty-Eight and No/100 Dollars (\$13,168) upon said note and mortgage, a second and subsequent note and mortgage were executed by the said Rand Truck Line, Inc., to and in favor of the said Markees purporting to bind the Bankrupt herein to pay the sum of Forty-Three Thousand Five Hundred and Sixty Dollars (\$43,560) which sum included said balance and the sum of Twenty-Two Thousand Two Hundred and Fifty-Eight Dollars (\$22,258) then paid by the said Otto W. Heider to and on behalf of the Rand Truck Line, Inc., Bankrupt herein and pre-paid interest on said sums. That said note and mortgage was forthwith delivered to the said Otto W. Heider that thereafter the said Markees and other agents of said Bankrupt continued to divert and cause to be diverted and paid to the said Otto W. Heider upon said second note and mortgage additional large sums of money in excess of Thirty-Two Thousand and Sixty Dollars (\$32,060) belonging to and owned by the Bankrupt herein.

### III.

That the bankrupt herein received nothing of value nor any consideration whatsoever in return for the execution of the first note and mortgage or payment of such personal obligations of the stockholders. That the money paid to and on behalf of the



Bankrupt herein at the time of the execution of the second mortgage constituted and was a partial repayment of the monies theretofore diverted from said corporation; that at the time of and after such partial repayment there remained a balance still due said corporation by reason of such diversion the sum of Two Thousand Two Hundred and Forty-Two Dollars (\$2,242); that all of the subsequent diversion of funds from the corporation and its creditors and the payment thereof to Otto W. Heider were to the detriment of its then existing creditors and for the individual use and benefit of the stockholders of said corporation.

#### IV.

That as a result of such payments so made and so received by the said Otto W. Heider a net sum of not less than Thirty-Four Thousand Three Hundred and Two Dollars (\$34,302) of monies owned by the said Bankrupt herein were diverted from said corporation and applied upon the aforesaid individual debts and obligations of the stockholders of the Bankrupt herein; that the said Otto W. Heider with full knowledge that such sums of money belonged to and were the assets of said Bankrupt corporation received and accepted the same and attempted to apply the same in payment of said personal obligations of the said stockholders; that no part of said sums have been repaid to the said Bankrupt or to the Trustee herein.

#### V.

During the period of time between September 28, 1944, and May 20, 1949, the Bankrupt herein did not

earn any profits, in excess of operating costs, and did not have nor acquire any surplus funds; that the debts and liabilities of said Bankrupt increased and continued to increase during said period, and remained unpaid to and including the date of adjudication in bankruptcy herein; that the monies so paid out and received as hereinabove found, were not paid out of net profits or surplus; that the execution of the said notes and mortgages and payment of the monies paid out and received as aforesaid, rendered and caused the Bankrupt herein to become and be insolvent and bankrupt and unable to pay its debts in the ordinary course of business, and with liabilities exceeding in amount the value of its assets, taken at a fair valuation and exclusive of such money so paid and received as herein found; that at the time of its adjudication in bankruptcy herein, the said Rand Truck Line, Inc., Bankrupt herein, was indebted to various firms and persons and corporations in a total approximate amount of Forty Thousand Dollars (\$40,000); that the claims of some of such creditors existed prior to August 7, 1946, and continued to exist subsequent to August 7, 1946, up to and including the time the petition in bankruptcy was filed herein; that the execution of said notes and mortgages and the payments of money paid out and received as hereinabove alleged, hindered, delayed and defrauded the creditors of the bankrupt herein and were intended to by the parties to such transactions and did deprive said creditors of the assets of said corporation and were intended to and did

attempt to discharge the personal obligations of the stockholders of the Bankrupt herein, to Otto W. Heider, to the detriment and damage to said creditors of said Bankrupt.

## VI.

That the Articles of Incorporation of the said Bankrupt give or grant to such corporation no power or pledge its credit or borrow for or on behalf of its stockholders, directors or any other persons whatsoever to purchase its own stock for or on behalf itself or any other person. That the execution of the said notes and mortgages and the payment of such sums as hereinabove alleged was and is beyond the power and authority of said corporation, its officers or directors.

## VII.

That there was included in each of said mortgages hereinabove described prepaid interest at a rate and in an amount in excess of 10% per annum; that the agreements of the Bankrupt herein to pay such sums representing prepaid interest were demanded and received by the said Otto W. Heider as the consideration for the extension of time evidenced by said notes and mortgages for the payment of said debts and were included and added to the balances claimed to be due from the Bankrupt to Otto W. Heider knowingly and with the intent on the part of the said Otto W. Heider to collect and receive and to have the said Bankrupt pay interest upon said indebtedness at a rate in excess of 10% per annum; that the said Otto W. Heider received and accepted said notes and mortgages with full knowledge of the

facts hereinabove stated; that the said Otto W. Heider has received out of the assets of this corporation, funds in excess of any monies advanced by him to any person whatsoever as the result of any transactions hereinabove set out; that the balance represented by the claim of the said Otto W. Heider filed herein was and is a balance representing only interest charges computed upon such sums so advanced at a rate in excess of 10% per annum.

### VIII.

That Otto W. Heider has not been prejudiced by any delay in filing objections to his claim herein.

Based upon the foregoing Findings of Fact, the Court draws the following:

### Conclusion of Law

The claim of Otto W. Heider herein, based upon said notes and mortgages, should be denied.

Dated this 1st day of October, 1956.

/s/ ESTES SNEDECOR,  
Referee.

Affidavit of service by mail attached.

[Endorsed]: Filed October 1, 1956, Referee.

[Endorsed]: Filed October 23, 1956, U.S.D.C.

In the United States District Court for the  
District of Oregon

No. B 29,990—In Bankruptcy

In the Matter of:

RAND TRUCK LINE INC., an Oregon Corporation,

Bankrupt.

### ORDER

Based upon Findings of Fact and Conclusions of Law made and entered herein on the 1st day of October, 1956;

It Is Ordered that the purported notes and chattel mortgages held by Otto W. Heider, upon the assets of the bankrupt herein be, and the same hereby are, held to be void and of no effect whatsoever, and

It Is Further Ordered that the claim of the said Otto Heider filed herein, based upon the claimed balance due upon said notes and mortgages be, and the same hereby is denied and disallowed in all respects.

Dated this 2nd day of October, 1956.

/s/ ESTES SNEDECOR,  
Referee.

[Endorsed]: Filed October 2, 1956, Referee.

[Title of District Court and Cause.]

### PETITION FOR REVIEW

To: The Honorable Estes Snedecor, Referee in  
Bankruptcy:

The petition of Otto W. Heider, respectfully  
represents:

1. That your petitioner is a duly qualified creditor of the above-named Bankrupt.

2. That on the 2nd day of October, 1956, an order was made by the Referee herein, and filed in this Court, a copy whereof is hereto annexed, marked Exhibit A, and made a part hereof.

Your petitioner, being aggrieved by the said order, prays for a review thereof, and complains that the Referee committed error in making the said order in the following particulars:

a. The Bankruptcy Court was and is without jurisdiction to entertain the objections to the claim of your petitioner, upon which said order is based, because the same matter was by the direction and authority of the Referee in Bankruptcy submitted to the jurisdiction of the Circuit Court of the State of Oregon, for the County of Multnomah, in the case of Samuel A. McAllister, Trustee in Bankruptcy for Rand Truck Line, Inc., a bankrupt, vs. Vern Markee, Florence Markee, his wife; Loren Markee, Harold Macy, Beryl B. Taylor and Otto Heider, being Docket No. 190-145 in said Court.

b. The Referee in Bankruptcy should not have considered the objections of the Trustee to the claim

of your petitioner, upon which objections said order is based, because there was undue laches upon the part of said Trustee which had a material adverse effect upon your petitioner, in that the Trustee was to file any objections to the claim which he had after the hearing in this cause on July 6, 1949, but did not do so for nearly seven years thereafter, and accordingly the stale objections should not have been considered at the subsequent hearing on March 14, 1956.

c. That said order is not, in fact or in Law, supported by the findings of fact entered herein by said Referee.

d. That all parts of said findings of fact, material to the claim of your petitioner, are not only clearly erroneous but also false, as shown by the record in this proceeding.

Wherefore, petitioner prays that said order be reviewed by a Judge of this Court and that the Referee promptly prepare and transmit to the Clerk thereof his certificate thereon, together with a statement of the questions presented and a transcript of the evidence taken at the hearing, together with all exhibits therein offered.

TOOZE, KERR, HILL,  
DOUGHERTY & TOOZE,  
/s/ WILLIAM E. DOUGHERTY,  
Attorneys for Petitioner.

Affidavit of Service by Mail Attached.

[Endorsed]: Filed October 10, 1956, Referee.

[Endorsed]: Filed October 23, 1956, U. S. D. C.

[Title of District Court and Cause.]

CERTIFICATE OF REFEREE ON PETITION  
OF OTTO W. HEIDER FOR REVIEW OF  
REFEREE'S ORDER OF OCTOBER 2, 1956

To the Honorable Judges of the Above-Entitled  
Court:

Estes Snedecor, the Referee in Bankruptcy in charge of this proceeding, hereby makes this his certificate on the petition of Otto W. Heider for a review of the Referee's order entered October 2, 1956, denying and disallowing the chattel mortgage claim of Otto W. Heider.

Questions Presented

The questions presented are set forth in the Petition for Review, which accompanies this certificate.

Facts

A brief chronology of the proceedings will form a vivid and helpful background to the jurisdictional and other controversies under review.

Rand Truck Line, Inc., was adjudged a bankrupt upon its voluntary petition filed May 20, 1949. Immediately Beryl B. Taylor was appointed receiver to continue the operation of the trucks until the appointment of a trustee at the first meeting of creditors held June 7, 1949, at which time Samuel A. McAllister was appointed trustee.

In order to preserve the going values of the operating permits and to curtail operating losses, the



trustee very promptly on June 20, 1949, filed a petition challenging the validity of Otto W. Heider's mortgage and requesting an order requiring Heider to appear on July 6, 1949, and show cause why the property of the bankrupt should not be sold free from liens, the proceeds to be impressed with such liens as the court should determine to be valid. Heider appeared at the hearing and asserted a mortgage on the tangible assets of the bankrupt, upon which he claimed a balance owing of \$11,500, plus accruing interest.

Following this hearing on July 21, 1949, the Referee entered an order authorizing the sale of the tangible assets and operating rights of the bankrupt free from the lien of the mortgage claimed by Otto W. Heider, and providing that the proceeds of the sale be impressed with the lien of such mortgage or claimed mortgage, the court expressly reserving the right and power to determine the validity or amount due upon such mortgage.

After advertising and upon due notice to creditors, the property was sold to Clement M. Risberg for \$20,000 cash. The order authorizing the sale free from liens entered September 1, 1949, provided that the proceeds of the sale shall be impressed with the liens found upon the personal property so sold "with this court reserving the power to determine the validity and amount of all such liens."

On the same day, September 1, 1949, the trustee promptly filed a petition alleging that certain stock-

holders of the bankrupt had converted corporate funds to their own use, and had applied them to the payment of personal obligations owing to Otto Heider. The trustee requested authority to institute an action in the State Court against the stockholders and Otto Heider for the recovery of said corporate funds. An order was entered on the same day authorizing action. Such an action was filed in the Circuit Court of the State of Oregon for the County of Multnomah on September 19, 1949. This case has been pending in the State Court for more than 7 years upon various motions and demurrers and is still not at issue.

The action in the State Court is for the recovery of corporate funds and only indirectly involves the question of the validity of the Heider mortgage. The trustee finally decided not to await the outcome of the litigation against the stockholders and to invoke the summary jurisdiction reserved to the Bankruptcy Court for the purpose of determining the validity of the Heider chattel mortgage. Consequently, formal objections were filed to the mortgage claim and were heard before the Referee on March 14, 1956. During the hearing Heider was requested to produce a photostatic copy of the original mortgage to be marked Exhibit 32 and was given the privilege of introducing additional evidence in connection with the Long note if he so desired. In view of the complicated facts, Mr. Boll-enback agreed to submit a written summary of the evidence and to file the trustee's memorandum of

authorities. This was done on March 27, 1956. In the absence of an answering brief to be filed by Mr. Dougherty, Mr. Bollenback addressed a letter to the Referee with a copy to Mr. Dougherty requesting that the court set a time within which any additional evidence must be produced and briefs submitted by Heider. On June 12, 1956, the Referee addressed a letter to Mr. Dougherty referring to Mr. Bollenback's letter of May 28 and stating that Mr. Heider had failed to furnish the photostatic copy of the original chattel mortgage and that Mr. Dougherty had not submitted a brief upon the questions of law involved in the hearing before the court on March 14, 1956. The Referee advised Mr. Dougherty that, unless a brief was filed on or before June 25, the Referee would proceed to make findings upon the record now before the Court. Mr. Dougherty telephoned for additional time which was granted to him but no brief was filed and no request was made for the introduction of further evidence or for oral argument. Finally, on September 10, 1956, findings of fact and conclusions of law were submitted by Mr. Bollenback and copies were transmitted to Mr. Dougherty with notice that the Referee would consider these findings on September 20, 1956, and that any objection thereto must be filed before that date. On September 18 Mr. Dougherty addressed a letter to the Referee stating that he was engaged in a trial in the Circuit Court in Pendleton and requested that the time for filing objections be set over until Tuesday, September 25. Nothing further was heard from Mr. Dougherty,

so on October 1, 1956, the Referee entered Findings of Fact and Conclusions of Law, and on October 2 entered an order denying and disallowing the chattel mortgage claim of Otto Heider. A copy of the order was immediately mailed to Mr. Dougherty.

### Papers Submitted

Transmitted herewith are the following papers:

1. Proof of Secured Debt.
2. Objections to Proof of Debt of Otto W. Heider, filed January 31, 1956.
3. Supplemental Objections to Claim of Otto Heider.
4. Motion to Dismiss, filed by William E. Dougherty, March 14, 1956.
5. Findings of Fact and Conclusions of Law, filed October 1, 1956.
6. Correspondence between counsel and the Referee.
7. Order Denying and Disallowing Chattel Mortgage Claim of Otto W. Heider.
8. Petition for Review, filed by Otto W. Heider, October 10, 1956.
9. Transcript of Proceedings before the Referee on July 6, 1949.
10. Transcript of Proceedings before the Referee on March 14, 1956.
11. Trustee's Summary of Evidence, filed March 27, 1956.
12. Trustee's Memorandum of Authorities, filed March 27, 1956.

13. Trustee's Exhibits 1 to 13, inclusive, introduced at the hearing before the Referee July 6, 1949.

14. Trustee's Exhibits 14 to 18, inclusive, 19 to 29, inclusive, and Exhibit 33.

15. Claimant's Exhibits 20, 30 and 31.

Dated at Portland, Oregon, this 23rd day of October, 1956.

Respectfully submitted,

/s/ ESTES SNEDECOR,  
Referee in Bankruptcy.

[Endorsed]: Filed October 23, 1956, Referee.

[Endorsed]: Filed October 23, 1956, U.S.D.C.

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[Title of District Court and Cause.]

### ORDER

This matter having come on to be heard on the petition of Otto W. Heider for a review of the Referee's order entered October 2, 1956, denying and disallowing the chattel mortgage claim of Otto W. Heider; and

It appearing that there is ample support for the findings of fact and conclusions of law dated October 1, 1956, and the Referee's order dated October 2, 1956; and the Court being fully advised in the premises;

It Is Hereby Ordered that the petition for review be denied and the order of the Referee is hereby affirmed.

Dated this 28th day of March, 1957.

/s/ GUS J. SOLOMON,  
United States District Judge.

[Endorsed]: Filed March 28, 1957, U.S.D.C.

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[Title of District Court and Cause.]

#### NOTICE OF APPEAL

Notice is hereby given that Otto W. Heider, a creditor of the bankrupt above named, hereby appeals to the United States Court of Appeals for the Ninth Circuit from the order entered in this proceeding and dated March 28, 1957, wherein the above-entitled District Court ordered that the petition for review filed by said creditor be denied, and that the order of the Referee thereon be affirmed.

WILLIAM E. DOUGHERTY,  
Of Attorneys for Said  
Otto W. Heider.

[Endorsed]: Filed April 29, 1957.

[Title of District Court and Cause.]

## BOND FOR COSTS ON APPEAL

Know All Men by These Presents, that we, Otto W. Heider, as principal, and Glens Falls Insurance Company, a New York corporation, as surety, are held and firmly bound unto said S. A. McAllister, Trustee in Bankruptcy for the above-named bankrupt, as obligee, in the sum of Two Hundred Fifty Dollars (\$250), for the payment of which well and truly to be made to the said obligee we do hereby bind ourselves and our respective executors, administrators, successors and assigns, jointly and severally, firmly by these presents.

The condition of this obligation is such that:

Whereas, said principal has heretofore filed a notice of appeal to the United States Court of Appeals for the Ninth Circuit from that certain order entered in the above-entitled proceedings on the 28th day of March, 1957, by the United States District Court for the District of Oregon.

Now, Therefore, if said principal shall prosecute his appeal to effect and pay all costs, if the appeal is dismissed or the judgment affirmed, or pay such costs as said appellate court may award if the judgment is modified, then this obligation shall be void; otherwise to remain in full force and effect.

In Witness Whereof, Otto W. Heider, as principal, and said Glens Falls Insurance Company, as

surety, have hereunto set their hands and seals this 3rd day of May, 1957.

/s/ OTTO W. HEIDER,  
Creditor and Appellant,  
Principal.

[Seal] GLENS FALLS INSURANCE  
COMPANY,  
A New York Corporation,  
Surety;

By /s/ [Indistinguishable],  
Attorney.

Countersigned:

JEWETT, BARTON, LEAVY  
AND KERN,

By /s/ [Indistinguishable],  
Resident Agent.

[Endorsed]: Filed May 9, 1957.

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[Title of District Court and Cause.]

### ORDER

Upon application of the appellant and good reason appearing therefor, as authorized by Rule 73(g) of the Rules of Civil Procedure, it is hereby

Ordered that the time for filing the record on appeal and docketing the appeal in this matter be, and hereby is, extended to and including July 8, 1957.



Done this 7th day of June, 1957.

/s/ GUS J. SOLOMON,  
Judge.

[Endorsed]: Filed June 7, 1957.

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[Title of District Court and Cause.]

### STIPULATION

It Is Hereby stipulated that the Court may extend the time for filing the record on appeal and docketing the appeal in this matter to and including July 27, 1957.

/s/ WILLIAM E. DOUGHERTY,  
Of Attorneys for Appellant.

/s/ C. X. BOLLENBACK,  
Of Attorneys for Appellee.

[Endorsed]: Filed July 3, 1957.

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[Title of District Court and Cause.]

### ORDER

Based upon the stipulation filed herein and good reason appearing therefor, as authorized by Rule 73 (g) of the Rules of Civil Procedure, it is hereby

Ordered that the time for filing the record on appeal and docketing the appeal in this matter be, and hereby is, extended to and including July 27, 1957.

Done this 3rd day of July, 1957.

GUS J. SOLOMON,  
Judge.

[Endorsed]: Filed July 3, 1957.

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[Title of District Court and Cause.]

ORDER

Based on the motion of the appellant, and good reason appearing therefor, it is

Ordered that the Clerk of this Court forward to the United States Court of Appeals for the Ninth Circuit, in connection with the appeal of the above-entitled cause, all of the original documentary exhibits in accordance with the usual practice of this Court in regard to the safekeeping and transportation of original documents.

Done this 19th day of July, 1957.

GUS J. SOLOMON,  
District Judge.

[Endorsed]: Filed July 19, 1957.

United States District Court, District of Oregon

B-29990

In the Matter of:

RAND TRUCK LINE, INC., an Oregon Corporation,  
tion,

Bankrupt.

July 6, 1949—10:00 A.M.

Before: Honorable Estes Snedecor,  
Referee in Bankruptcy.

Appearances:

MR. CLARENCE X. BOLLENBECK,  
Attorney for Trustee;

MR. S. A. McALLISTER,  
Trustee;

MR. MOE M. TONKON,  
Attorney for Bankrupt;

MR. BERYL TAYLOR,  
Manager, Rand Truck Line, Bankrupt;

MR. OTTO W. HEIDER,  
Creditor, in His Own Behalf;

MR. and MRS. VERN MARKEE,  
Witnesses;

MR. JOHN HICKSON,  
Attorney for Vern Markee.

## PROCEEDINGS

Proceedings in re Examination of Otto W. Heider  
and Vern Markee:

The Referee: This is the time set for the hearing of the order requiring Otto Heider to assert his claim of lien against certain assets belonging to the bankrupt estate. Mr. Heider has already filed, under date of June 30th, 1949, as required by the order a proof of secured debt in which he states that the bankrupt is indebted to him in the sum of \$11,500, being a balance due on notes and mortgages outstanding and existing on the 7th day of August, 1946. I suppose that means notes and mortgages dated as of that date. And to it is attached a mortgage dated August 7, 1946, made by the Rand Truck Line, an Oregon corporation; Vern Markee and Florence Markee, his wife, as the mortgagors, and H. H. Macy and Vern Markee, Florence Markee and Loren Markee, as mortgagees. Is that right?

Mr. Heider: Yes.

The Referee: This mortgage is given to secure an obligation of \$43,560 and it includes a piece of real estate in Morgan's Addition to the City of Sheridan and certain trucks and trailers and other equipment of the Rand Truck Line, and a long list of furniture, fixtures and equipment belonging to the Rand Truck Line. There is also attached the original note dated August 7th, 1946, executed by Rand Truck Line and Loren E. Markee in which they promise to pay to the order of H. H. Macy, Vern Markee, Florence Markee and Loren Markee

at [2\*] McMinnville, Oregon, \$43,560 with interest thereon at the rate of 8 per cent per annum from maturity until paid, payable in monthly installments not less than \$1,000 each, together with full amount of interest due on this note at the time of payment of each installment.

Mr. Heider, this appears to be an executed copy of the mortgage, but it does not have a filing mark on it.

Mr. Heider: I think there is one on file, too, in Multnomah County. They are recorded.

The Referee: In Multnomah County?

Mr. Heider: Yes.

The Referee: It was executed in duplicate?

Mr. Heider: Yes.

Mr. Tonkon: You mean Multnomah County or Yamhill County?

Mr. Heider: Both counties.

The Referee: Now, at the time Mr. Heider sent up this proof of claim he wrote me a letter in which he asked whether it would be necessary for him to appear today in view of the fact that he had filed his proof of claim, and I wrote acknowledging receipt of the claim and of his letter. I said, "The claim is deficient in that you did not include therein an itemized statement of monies disbursed or received by you in connection with any transactions or payments made in connection with said mortgage or the prior mortgage executed September 18, 1944." In that I was following the language [3] of the

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\*Page numbering appearing at top of page of original Reporter's Transcript of Record.

order. I said, "Please bring such a statement with you at the hearing scheduled in my courtroom on Wednesday, July 6, 1949, at 10:00 o'clock a.m. Also bring with you your original record showing receipts and disbursements in connection with the two mortgages. The hearing set for next Wednesday is for the purpose of receiving proof of the balance due on your mortgage and of all transactions in connection with it so that the Court may determine the validity of the mortgage and the amount owing thereon."

Now, you may proceed. I think possibly the best procedure, Mr. Heider would be for you to take the stand and produce the information and let counsel examine you in connection with it, and if you will just bring your briefcase up here and have a chair.

#### OTTO W. HEIDER

was thereupon produced as a witness in his own behalf and, being first duly sworn, was examined and testified as follows:

The Referee: Do you have a summary or itemized statement?

A. Well, I brought these vouchers of disbursement on the first mortgage. That is the vouchers made to Mr. and Mrs. Rand. I thought they might want to look them over.

#### Direct Examination

By Mr. Bollenbeck:

Q. You don't have an itemized statement as suggested by the order? [4]      A. That is it.

(Testimony of Otto W. Heider.)

Q. You don't have an itemized statement?

A. Yes, I do have.

Q. Where is it?           A. This is it.

Q. Do you have an itemized statement of the receipts of these monies?

A. You mean on the first mortgage?

Q. On both of them.

A. Well, I have—the first mortgage, I gave that back to Mr. Taylor. He has that.

Q. I am asking you about an itemized statement of the payments received and made by you.

A. On the first?

Q. On both of them.

A. You have the first one, the disbursements.

The Referee: Those are disbursements. We want to know what was received.

A. Here is a statement of the receipts on the first mortgage right there.

Q. (By Mr. Bollenbeck): This is your original record?           A. Yes; it is my original record.

Mr. Bollenbeck: Will you mark this?

(Document bearing title, "Payments by Mar-  
kee," so produced, was thereupon marked  
Trustee's [5] Exhibit 1.)

Q. (By Mr. Bollenbeck): Now, Mr. Heider, without me leafing through all these checks, can you tell me how much you disbursed on the mortgage?

A. \$36,500. That is, you mean on the Rand mortgage, the first mortgage?

Q. The first mortgage.

(Testimony of Otto W. Heider.)

A. I think it is \$36,500. I think that is a pretty close figure.

The Referee: You bought the Rand mortgage, didn't you?

A. Yes; I bought the Rand mortgage from Mr. and Mrs. Rand and Mr. Bollenbeck has it there.

Q. (By Mr. Bollenbeck): When did you buy it?

A. The date of the first check there. You have it there. Well, the date of the mortgage—if you give me the mortgage I can give you the exact date there if you like. I bought the mortgage shortly after this was executed, shortly after September 28, 1944.

Q. Did you prepare that mortgage?

A. Well, I prepared most of it. I think Mr. Rand had some attorney prepare some of it here in Portland, or check it, I don't remember just what.

Q. You prepared it, though, and then it was turned over to Mr. Rand's lawyer and checked?

A. Yes; he checked it. [6]

Mr. Bollenbeck: This is going to be a job, your Honor, checking through these checks, and I hesitate to take the time of the Court to do it at this time. I think that I would like to offer them in evidence as they stand and check them over at a later date.

The Referee: Well, you have some other questions?

Mr. Bollenbeck: Yes; I do, your Honor.

A. I think, Mr. Bollenbeck, there is a slip there attached to them.

Mr. Bollenbeck: Let me put them in evidence.



(Testimony of Otto W. Heider.)

(Sheaf of checks, so produced, was thereupon marked Trustee's Exhibit 2.)

The Referee: Does Exhibit 2 represent your checks, what you paid out for the mortgage?

A. What I paid out to the Rands for the mortgage. I think they are all there, although I am not certain.

The Referee: What is the amount you paid?

A. I think it is \$36,500, although I am not sure that is exactly accurate, but I think it is very substantially so, but I had difficulty in finding some of those old cancelled checks. It is five years old.

The Referee: Well, do you remember what your agreement was when you bought it?

A. Remember what?

The Referee: How much did you agreed to pay for it? [7]

A. That was it; that was correct.

The Referee: \$36,500?

A. \$36,500.

Q. (By Mr. Bollenbeck): Mr. Heider, don't you have a ledger sheet on a transaction of this size?

A. This is what I kept on this.

Q. This yellow sheet, Exhibit 1?

A. That was the original record. That was the original record, that is what you asked for.

Q. You didn't enter the payments into a cash book or anything else when you received them?

A. I didn't have a cash book. That was my record right there.

(Testimony of Otto W. Heider.)

Q. You didn't have any ledger to show the amount due on the mortgage?

A. A ledger to show the amount due—yes; that shows the amount due all the time right from the beginning.

Q. In other words, this yellow sheet, Trustee's Exhibit 1, is your sole and only record of this transaction, is that right?

A. That is my original record.

Q. What other records do you have?

A. I don't have any other with me, but that is what you asked for, my original record.

Q. What other records do you have?

A. Well, I have the cancelled checks. I gave them to you and you introduced them in evidence. [8]

Q. Yes. And what other records do you have?

A. I don't know that I have any others.

Q. No records at all?

A. Yes. I have the mortgage and I gave it to Mr. Taylor, and I gave the checks to you and you introduced them in evidence.

Q. Do you have any other records?

A. Not that I know of.

Q. Well, you would know of any others you have?

A. Well, I have some copies here of some checks, but those are not signed. Those are not originals. You asked for originals.

Q. Do you have any sort of a ledger sheet you carried on this transaction?

A. No ledger sheet. That is the transaction. Here

(Testimony of Otto W. Heider.)

is some copies. I don't think they would be of any value. They are not signed.

Q. Well, now, Mr. Heider, you knew when this first mortgage was prepared that you were going to end up owning it, didn't you?

A. No, I didn't know it at all; didn't know it at all.

Q. You didn't have any idea that you might be buying it?

A. I didn't know. Rand told me that he might want to sell it.

Q. Were you attorney for Rand?

A. No; I wasn't.

Q. Were you attorney for Markee? [9]

A. No; I wasn't.

Q. Then why does it happen that this mortgage provides that all insurance policies now on file with the Public Utilities Commissioner of the State of Oregon shall be left in the safekeeping of Otto W. Heider of Sheridan, Oregon?

A. You say why would they be left there?

Q. Yes. A. Well, I had a safe in my office.

Q. You didn't have any idea of buying this?

A. We hadn't made any deal on it yet; we hadn't closed up any deal on it.

Q. Before it was executed?

A. No, no. You mean I bought it before it was executed?

Q. Yes. A. No.

Q. Why was this inserted in here then, why was this provision in the mortgage?

(Testimony of Otto W. Heider.)

A. In the mortgage?

Q. Yes.

A. Well, I had probably been looking after it for Mr. Rand. He didn't hire me though but I probably was——

Q. How did it happen it was prepared in your office?

A. Oh, I was doing some work in my office and the parties were there and it was convenient. Mr. Rand was in town every week and it was a convenient location. [10]

Q. You didn't represent him as his lawyer?

A. I don't think Mr. Rand ever paid me a dollar attorney's fees.

Q. And you didn't represent Markees?

A. Oh, the Markees have had some legal work off and on, small amounts at different times, that I have done for them.

Q. Well, whom did you represent when you prepared this mortgage?

A. Well, I represented Mr. Rand.

The Referee: Did you represent the truck line?

A. No; I didn't. He had a firm of attorneys here in Portland, and I can't tell you who they were.

Q. (By Mr. Bollenbeck): Did you prepare the minutes of the meeting?

A. No; they had—I think Mr. Rand or Mrs.—they had somebody to keep the minutes of the meeting. I think I did type up some minutes of the meeting.

Q. You didn't type them up?

(Testimony of Otto W. Heider.)

A. Oh, I think some part of the minutes, not all of them.

Q. You didn't represent yourself in this transaction when you were preparing this mortgage?

A. Well, if I did anything, I didn't ignore myself, that is for sure.

Q. And you knew you were going to buy it?

A. Well, we talked about it, but we hadn't come to any meeting of minds. We had discussed it, that is right, we had discussed [11] it.

Q. Who computed the amount of interest and arrived at this figure of \$43,560?

A. Well, I imagine all parties involved did.

Q. Including yourself?

A. Well, I was there. I think all parties involved had a hand in it.

Q. Now, Mr. Heider——

(Promissory note, dated September 28, 1944, payable to Mrs. R. R. Rand and signed by Vern Markee, Loren E. Markee and Florence Markee, so produced, was thereupon marked Trustee's Exhibit 3.)

Q. (By Mr. Bollenbeck): Did you buy this mortgage at——

A. The interest was figured in and I bought it at a discount of the interest.

Q. You say you paid \$36,500 for it?

A. Yes; approximately right.

Q. And is that what the Rands were selling their stock to the Markees for?

(Testimony of Otto W. Heider.)

A. Oh, I don't know what they sold the stock to Markee for.

Q. What was the consideration for this mortgage?

A. Well, I just give you the cancelled checks a little bit ago.

Q. I know. Between the Rands and the Markees what was the consideration for the mortgage? [12]

A. They made their own deal. You would have to see Mr. Rand and Mr. Markee. You mean what the total sales price of the truck line was? I can't tell you that.

The Referee: Well, was this mortgage, did it represent all or part of the purchase price?

A. I understood it represented part, not all, of the purchase price. Now, as near as I can answer your question, is that I understood the sales price was somewhere between fifty and sixty thousand, the original sales price. As to that, I don't know, but that is my impression of the whole thing. What the original sales price and what that was, I can't give you that. I can't remember. It might have been discussed five years ago in my presence, but just what those figures are, I don't know.

Q. (By Mr. Bollenbeck): I will hand you Trustee's Exhibit 3 for identification, which is the original note signed by Vern Markee and Florence Markee and endorsed by Mrs. R. R. Rand without recourse or liability, and ask you why that kind of an endorsement was put on there?

A. You would have to see Mrs. Rand about that

(Testimony of Otto W. Heider.)

because I imagine that is the way she wanted it. Why she put it on there you would have to consult her.

Q. Why did you accept it that way?

A. Why did I have to accept it any particular way?

Q. Why did you accept it that way? [13]

A. Well, what way did you want me to accept it?

Q. I mean, if this was a bona fide sale of this mortgage after it was executed, why did you accept that kind of an endorsement?

A. Well, I have accepted those kinds of endorsement lots of times. Why shouldn't I?

Q. Why did you?

A. Because I accepted it.

Q. As a matter of fact, Mr. Heider, you knew you were going to finance this mortgage before it was executed?

A. No; I didn't know anything about it. I knew we talked about it but I couldn't guarantee I was going to buy it; I couldn't guarantee it at all.

Q. Who is Irene Lawrence?

A. She is a stenographer in my office.

Q. She notarized this mortgage?

A. Yes; she did; that is her signature.

Q. The mortgage is dated September 28, 1944. Now, when did you—when was it assigned to you?

A. Well, you must have the assignment there. If you will hand it to me I will read the date for you.

Q. I have an assignment of the second mortgage but not of the first.

(Testimony of Otto W. Heider.)

A. Well, I think Mr. Taylor got it all together so it must be over in his office. [14]

Q. Well, considering the date of execution of September 28, 1944, when was it assigned to you?

A. Well, the assignment will speak for it on it. I can't tell you because I think Mr. Taylor got it with the mortgage and you will have to get it from him.

Q. Did you record the assignment?

A. I don't remember whether the assignment was recorded or not. My impression was that it was not recorded, although I wouldn't be sure.

Q. How long before you made your first payment to the Rands was the assignment taken?

A. Well, from the cancelled checks——

Q. Just answer the question.

A. Oh, I don't remember five years ago. I can't remember, nor neither would you.

Q. Was the assignment made simultaneous with the first payment?

A. I don't recall. If you got the assignment I can tell you; if you will produce the assignment, and that will refresh my memory five years back, but I can't do the impossible.

Q. You have the assignment as far as I know.

A. No; I haven't got it. Mr. Taylor has.

Q. When did you decide to buy this mortgage?

A. Shortly after it was executed. That is what I told you.

Q. How shortly after?



(Testimony of Otto W. Heider.)

A. I don't know. I can't give you the hour or day. [15]

Q. Was it within twenty-four hours?

A. I wouldn't say. It might have been forty-eight hours.

Q. Might have been forty-eight hours?

A. Might have been a week or two weeks, but I think the assignment will show pretty well. That is perhaps a copy of the assignment you have there.

Q. That is the second mortgage.

A. If you will show me the date of the first check there——

Q. I just want you to fix the date of the assignment without seeing the first check.

A. I can't fix the date five years. Can you remember any transaction that happened in your office, the date and hour, five years ago?

Q. Well, if it involved \$43,500 of my money I would.

A. Well, you are a lot smarter than I am; I will give you credit for that.

Q. Now, Mr. Heider, you knew what this transaction involved, that it was at least part payment of the stock of the Rand Truck Line?

A. Oh, I realized it was payment of most of the tangible assets of the Rand Truck Line. That was my understanding.

Q. Well, that was symbolized by a sale of the stock, wasn't it? The assets themselves were not sold to anybody?

A. Yes; I suppose symbolized by the stock.

(Testimony of Otto W. Heider.)

Q. So it was a sale of the capital stock of the Rand Truck [16] Line?

A. Yes. I understand Mr. Rand parted with all his interest in the Rand Truck Line. I understood he was entirely out.

Q. And did you take the capital stock as additional stock for security of this mortgage?

A. I think I had the original stock, and I have the new stock now. Now, the original stock—I can't tell you where that is. I think that was returned, most of it, to Mr. Taylor and the different ones, the different parties, and then was taken up by the new stock. Now, I can't tell you what parties got that stock but there was four or five different ones that got the old original stock, but I have the new stock here with me today.

Q. Now, you knew that this money that was being paid out to the Rands on this mortgage and would be repaid to you by the corporation?

A. Yes, by the corporation.

Q. That it was in payment of a debt that the corporation didn't owe?

A. It was payment of a debt the corporation didn't owe?

Q. Yes.

A. Well, of course, I understood it was a debt the corporation did owe, so I was——

Q. Well, you knew it was part of the purchase price of the sale of this stock, didn't you? You stated that. [17]

(Testimony of Otto W. Heider.)

A. Well, it was of all the tangible assets of the corporation. I knew that.

Q. Now, Mr. Heider, you are a lawyer and you know there is a lot of difference between the sale of the assets of the corporation and the sale of the capital stock.

A. I don't practice law enough—you do all the time, you are in court probably ten times as much as I am, but I don't practice in court enough to—to sell the tangible assets and the stock, it means the same thing to me, because you are passing over all the tangible assets when you sell. It means the same thing to me.

Q. You know the physical assets of this corporation did not change hands as a result of this transaction, they were still owned by the Rand Truck Line, weren't they?

A. The management and personnel and all changed hands.

Q. The tangible assets were still owned by the same corporation that owned them prior to this transaction, weren't they?

A. There was a change made in the corporation there and I can't tell you what that was. There was a change made in the corporation at that time.

Q. Now, just answer my question.

A. Well, the business continued as before.

Q. Yes.

A. Yes, that is right. The same assets were operated, the same rolling stock. [18]

(Testimony of Otto W. Heider.)

Q. There was no transfer of title of the tangible assets of the Rand Truck Line, was there?

A. Well, I think there was. I think the certificates of title were transferred.

Q. To whom?

A. They were transferred on the records of the Secretary of State's office.

Q. To whom? A. To the Rand Truck Line.

Q. Who had owned them prior to that time?

A. Some of the titles were in Rand's name individually, R. R. Rand, and they were transferred over to the Rand Truck Line.

Q. Was that part of the consideration for this transaction?

A. Well, it was handled all substantially at the same time so I suppose it was part of the whole transaction, yes.

Q. And how many years have you practiced law, Mr. Heider? A. Thirty-five.

Q. And you are sitting up there and telling me that that is what your conception of this transaction is?

A. Yes. When you transfer all the stock it amounts to the same thing as transferring all the assets of any corporation. Yes. That is my idea of it, that you can't sell the assets to one person and stock to another person of any corporation, you can't split up that way; it won't work.

Q. Now, Mr. Heider, can you tell us from whom these payments [19] were received?

A. Well, they were received from the Rand

(Testimony of Otto W. Heider.)

Truck Line, from the earnings of the Rand Truck Line, that is right.

Q. Do you know whether any of the officers or directors of the Rand Truck Line had any outside income?

A. Mr. Macy over there, or whether Loren Markee had any outside income, I don't know. Whether they had any other business, I don't know.

Q. Well, you stated emphatically it came from the earnings of the Rand Truck Line.

A. And so far as I knew, that was my information.

Q. You don't know who paid them to you?

A. Oh, whoever happened to be the manager at the time. Mr. Taylor paid—I don't know whether he was the manager—I don't think he was in the beginning, but when he became manager he paid the payment and prior to that time whoever was in charge paid them.

Q. Now, can you tell me from this Trustee's Exhibit 1 what the balance was at the time of refinancing?

A. \$13,168.

Q. All right; now, let's get down to the second transaction. Have you got the original of the second mortgage?

A. Well, I think the Court—yes—has it there. I have a substantial copy of it.

Q. Now, what disbursements did you make when you took the [20] second mortgage?

A. Well, here is the cancelled vouchers right

(Testimony of Otto W. Heider.)

here. That was a certified check. There you are. You better put this with it.

Q. \$13,168?

A. I believe that is correct. I think you have an adding machine tape there on it, the same figure.

Q. You have handed me a First National Bank of Sheridan, Oregon, statement dated August 7, 1946, representing the certified check to Rand Truck Line for \$5,000.

A. That is right.

Q. Also a check dated August 7, 1946, to the Rand Truck Line, Inc., and Transport Bodies & Equipment Company for \$3,000, a check, the Rand Truck Line, dated August 7, 1946, for \$5,000, and a check to the Rand Truck Line for \$4,508 dated August 14, 1946. Now, that, those total, those four items total \$17,508, and you have a balance of \$13,168. That is a total of \$30,706, according to my computations. Now, how did you arrive at the rest of the balance of this \$43,560 on the second mortgage?

A. I think you made a mistake in your computation. Yes, you have.

Q. I will be glad——

A. You add it again and you will find your total is \$36,027.

Q. I noticed on your adding machine data you have more than four items and now you have only delivered the evidence of four of them. [21]

A. I don't know what item—you got the items there. This is one of the items right here, and this one here, and there they are, that makes the correct amount.

(Testimony of Otto W. Heider.)

Q. Now, in addition to these four checks that you have submitted to me you have submitted a chattel mortgage payable to Earl Walden or Otto W. Heider upon certain equipment with the principal of \$1,080.

A. That was taken up at the time of the second mortgage.

Q. Who is Earl Walden?

A. Earl Walden?

Q. Yes. A. I don't know him.

Q. You don't know him?

A. Earl Walden?

Q. Walden (spelling), W-a-l-d-e-n.

A. I think he might be an employee of Rand Truck Line.

Q. Why was the mortgage made payable to him or to you?

A. Well, that was to either one of us.

Q. Why? A. Why not?

Q. Just answer the question without arguing with me. You are a witness here today, not a counsel.

A. I guess the mortgage can be drawn any way you want to draw it.

Q. Why was it drawn that way?

A. I don't know except that it was drawn that way. [22]

Q. Who drew it?

A. Hand me the mortgage. Maybe I can tell you. Earl Walden. I think he was an employee of the truck line. The note is just Earl Walden. Earl

(Testimony of Otto W. Heider.)

Walden is not named in the mortgage—or—I am not named in the note.

Q. Now, was that mortgage drafted in that fashion?

A. It subsequently was transferred to me, or I took it at the time.

Q. Well, did you advance any money on it?

A. Why, I did advance money on it.

Q. I mean when it was originally executed?

A. Well, now, on the date of my advance I can't tell you, but I did some time in the month of July, 1946——

Q. Prior to the time it was included in this second mortgage?      A. Yes; that is right.

Q. How much money did you advance on it?

A. Oh, I think \$1,050, \$1,050.

Q. To whom did you advance it?

A. I think Rand Truck Line.

Q. Do you have the voucher on that?

A. No; I couldn't find the voucher on that; I don't have——

Q. You don't have that cancelled check?

A. No; I don't have that cancelled check with me.

Q. Do you have it at Sheridan?

A. I don't know. I couldn't find it when I went through my [23] files yesterday.

Q. Who arranged for this mortgage for the Rand Truck Line?

A. Well, H. H. Macy, general manager at the time.



(Testimony of Otto W. Heider.)

Q. Do you remember that is who it was or is that what you are taking from the document?

A. That is Mr. Macy's signature. I think I am familiar enough with his signature to know that is it.

Q. He came to your office and wanted to arrange the loan? A. I think that is right.

Q. And your office prepared this mortgage, didn't it? A. I think it did.

Q. Miss Lawrence is on as Notary Public?

A. Yes.

Q. Now, why was the note and mortgage taken in the name of Earl Walden?

A. Well, Earl Walden had something to do with it, and I can't tell you just what he had to do with it at the time. I didn't know Earl Walden too well. I think I had met him, and just who he is I can't tell you at the moment.

Q. On these mortgages with prepaid interest, what interest did you compute that prepayment at?

A. Oh, the interest I think was computed on the basis of 10 per cent per annum compounded semi-annually.

Q. 10 per cent per annum compounded semi-annually? A. Yes. [24]

Q. This is a mortgage dated July 7, 1946.

Mr. Tonkon: Not the basic mortgage.

Q. (By Mr. Bollenbeck): The same interest rate? A. Yes.

Mr. Tonkon: But the interest was included in the outset in the basic mortgage, that is my point.

(Testimony of Otto W. Heider.)

Mr. Bollenbeck: Yes, only after maturity.

Q. Now, Mr. Heider, I am going to hand you a note and mortgage given apparently by the Rand Truck Line, rather to Rand Truck Line by Vern Markee and ask you to explain that mortgage.

A. Oh, that was a mortgage that was taken up at this—this is a mortgage that was taken up in that second mortgage you mentioned.

Q. Now, how did you happen to get that mortgage?

A. I suppose it was left with me when that second transaction was taken care of, when that second mortgage was made.

Q. Do you mean in that second mortgage that you bought that mortgage off of Vern Markee?

A. This balance was deducted out on that second mortgage, that is right.

Q. Now, let me get this straight. This is a mortgage that Vern Markee gave to the Rand Truck Line, right?

A. Yes; individually; he executed it individually.

Q. And then did you buy this mortgage from the Rand Truck Line?

A. I bought the mortgage. [25]

Q. When?

A. Well, shortly after its execution.

Q. Well, now, how shortly after its execution? It was executed in your office.

A. Oh, I suppose two or three days.

Q. As a matter of fact, it was simultaneous, wasn't it?

A. Well, very shortly afterwards.

(Testimony of Otto W. Heider.)

Q. That was done with the intention of you buying that mortgage?

A. Well, you mean that I give him the money with the intention of passing it to him?

Q. You knew you were going to pay out the money at the time you executed the mortgage?

A. Yes; on that mortgage I am sure I did.

Q. And how much did you pay for that?

A. Oh, I think about \$5,100.

Q. Did you have the cancelled vouchers for that?

A. No; I didn't find the cancelled voucher for that.

Q. Do you keep all your cancelled checks in one place?

A. No—well, I keep them in the back room in files. That had a balance on—that one at the time the second mortgage was written—I think it is written on the note there.

Q. You mean you lost your October, '45, and November, '45, cancelled vouchers?

A. Well, I don't think they are lost; I think they are misplaced. I am not sure that they are lost. [26]

Q. Do you remember exactly how much money you paid Rand Truck Line for this mortgage in the beginning?

A. I don't remember exactly.

Q. How was it paid? Was it paid in cash?

A. Cash and check.

Q. Well, now, do you mean you paid some of it in currency?

(Testimony of Otto W. Heider.)

A. Some of it in currency and some of it by check.

Q. Do you ordinarily do business with currency?

A. Oh, I do quite frequently where I have something to show for it.

Q. And then we have here, Mr. Heider, a conditional sales contract whereby the Rand Truck Line has purchased from you—wait a minute.

A. You are mistaken.

Q. Let me get this straight. This conditional sales contract, dated April 9, 1946, wasn't the Rand Truck Line buying that Fruehauf truck from you, or semi-trailer?

A. Yes; they were buying this from me. There is a balance on this one. You have it here.

Q. What is the balance on this?

A. \$1,721. That is on the 7th day of August, 1946.

Q. And that was at the time the second mortgage was made?

A. Yes; that is the time the second mortgage was made.

Q. Now, referring back again to this Vern Markee note and mortgage to the Rand Truck Line that you bought from the Rand [27] Truck Line, apparently that shows a balance of \$2,550 as of the date of the second mortgage.

A. Yes, that is right. And this shows a balance as of that date of \$1,721.

Q. And this Earl Walden note and mortgage,

(Testimony of Otto W. Heider.)

what was the balance on that at the time of the second mortgage?

A. Well, I guess there had been nothing paid on that, no part paid on that.

Q. And you figured that in at \$1,080?

A. I think it is on the slip there. You have it.

Q. For \$1,080 on your slip when you wrote the second mortgage, is that right?

A. If you will hand me the slip. That is right.

Q. Now, these items that we have been referring to, this certified check slip for \$5,000, this check to Rand Truck Line and Transport Bodies for \$3,000, the check to Rand Truck Line for \$5,000 and the check for Rand Truck Line for \$4,508, and \$1,080 on the Earl Walden note and mortgage, \$2,550 on the Vern Markee note and mortgage, and \$1,721 on the conditional sales contract, that is what was taken up in the second mortgage?

A. Yes; that is right.

Q. How did you happen to buy this or sell this Fruehauf trailer to Rand Truck Line?

A. You mean why did I sell it?

Q. Where did you get it before you sold it to them? [28]

A. I can't tell you where it came from.

Q. Was it Rand Truck Line's equipment?

A. Well, I don't know whether it was Rand Truck Line equipment or not. I'd have to trace the ownership of that, that is the prior ownership, through the Secretary of State's office, which could be done very well. Whether I bought it direct from

(Testimony of Otto W. Heider.)

Fruehauf or not, I couldn't tell you about that. It is possible that I did. It is in '45 so I might have bought it from Fruehauf.

Mr. Bollenbeck: I would like to offer these documents in evidence, your Honor.

The Referee: Put them all together with the adding machine tape and we will offer them as one exhibit.

(Mortgage dated July 11, 1946, and accompanying papers, so produced, were thereupon marked Trustee's Exhibit 4.)

Q. (By Mr. Bollenbeck): Now, Mr. Heider, you show a balance of \$36,027 as being these items to which we have just referred. The second mortgage is \$43,560, is that right? A. That is right.

Q. What is the difference, what represents the difference between those two figures?

A. The interest.

Q. Now computed at what rate?

A. At 10 per cent compounded [29] semi-annually.

Q. Now, among these items that you have stated is included this Earl Walden note dated July 11, 1946, in the amount of \$1,080, is that right?

A. Yes; that is included in the second mortgage.

Q. And that mortgage is dated July 11th, 1946, about 28 days prior to the execution of the second mortgage, is that right?

A. Yes; something like that.

(Testimony of Otto W. Heider.)

Q. And that Earl Walden mortgage provides for payments over a period of one year, is that right?

A. That is right.

Q. And in this \$1,080 that you have made this note for, it includes prepaid interest for the year?

A. That is right.

Q. Now, this Vern Markee mortgage is dated October 31, 1945, is that right, and there is a balance on it at the time of the second mortgage of \$2,550, is that right?

A. I think so, yes, a balance on it on August 7th, 1946—that is about a year after its execution—that is right.

Q. And that mortgage, note and mortgage, also provides that it shall run a year?

A. It did run a year, about.

Q. It provides for payment thereof in monthly installments?

A. That is right.

Q. And twelve monthly installments. And interest was computed in advance on that note and mortgage, too, was it not? [30]

A. I think so.

Q. And that the yearly period had not run on that note and mortgage before it was incorporated in this mortgage of August 7th had it either?

A. Almost.

Q. Not quite?

A. But there were a lot of delinquent payments from overdue interest on it. There was overdue interest on delinquent installments.

Q. Just a minute, Mr. Heider. From August 7,

(Testimony of Otto W. Heider.)

1946, to October 31, 1946, that period of the mortgage had not run yet?

A. No, that two months had not run.

Q. Now, Mr. Heider, when you took this second mortgage, at that time did Vern Markee owe you any money personally?

A. Oh, at that time I don't recall whether he did or not. He might have owed me some.

Q. Did you hold a mortgage on any of his property at that time?

A. Well, now, he might have—I did sell him and Mrs. Markee a house but what date I sold it to them—where they now live—I don't remember the date of that. They still owe me some on their residence yet, and I can't tell you the date of sale of the house, and if the date of sale of that house was prior to August 7th they did owe me on the house.

Q. Well, now, how much did you sell them the house for?

A. I think it was \$8500 or \$9000. [31]

Q. Well, Mr. Heider, don't you know?

A. Do you know every transaction you transacted in your office in the last three years? You don't know and you know you don't. Do you keep every item that you transacted in your office in your mind?

Q. Wasn't this formerly your home?

A. Yes, I lived there, but I didn't move the home away from there where it was located.

Q. Don't you remember what you sold your home for?

A. Well, I think it was \$8500 or \$9000, I



(Testimony of Otto W. Heider.)

wouldn't say which. I don't carry all those things in my mind and I don't think you do either. It don't make sense.

Q. How much is due and owing on that home now? A. Well, I can tell you approximately.

Q. All right, tell me approximately.

A. I think about \$6000, although I am not just sure. That is very close, though.

Q. Is that in the form of a conditional sales contract or mortgage?

A. Conditional sales contract.

Q. Conditional sales contract?

A. I think that is right.

Q. Are the payments being made promptly?

A. Yes, very good, no objection at all.

Q. Did you ever receive any checks from Rand Truck Line in [32] payment of that house?

A. No, I think Mr. Markee made them all individually, I am sure he did.

Q. Now, what is the legal description of that house, do you know what addition it is in?

A. Yes, it is in Block 11, Falkner's Addition, Sheridan. That description is by metes and bounds because it is a block divided up by metes and bounds and isn't platted off into lots. It is right across from the Catholic Church in Sheridan, across the street.

Q. Now, Mr. Heider, when you executed this second mortgage, in addition—first of all, let me ask you this: Did you prepare this second mortgage in your office?

(Testimony of Otto W. Heider.)

A. I think it was prepared in my office.

Q. Will you tell me why the mortgage was executed in the form it is in that it wasn't a direct mortgage from the Rand Truck Line to you?

A. Well, one of the reasons on that—for the same reason the banks execute the mortgage in the same manner so there is individual liability there. The banks, U.S. and First National both are using the same form, to get individual liability. I take it that is the reason.

Q. Is that why the original mortgage was made to Mrs. R. R. Rand?

A. Oh, Mr. and Mrs. Rand were the original owners.

Q. But, I know—— [33]

A. There was no—I don't think when they sold there was any outside stockholders.

Q. Is that why the original mortgage that you held was made payable to the Rands instead of to you?

A. They were the sellers.

Q. Why did you prepare the original mortgage to Rands instead of to you?

A. That is the way they wanted it prepared.

Q. But this second mortgage was executed to the Macys and Markees by the Company and then transferred to you so that you would have the individual liability of the stockholders, is that right?

A. Yes, they were the principal stockholders at that time, all of them, or, in fact, I think they were the only stockholders.

(Testimony of Otto W. Heider.)

Q. Why did you include this property in Morgan's Addition?

A. Well, that was where the terminal was located, if I recall.

Q. Whose terminal?

A. Well, Mr. Markee's terminal. That terminal never was owned by the Rand Truck Line.

Q. Is that Markee's terminal?

A. It is Markee's individual terminal.

Q. Markee was mortgaging his terminal to himself and you were buying the mortgage, is that the way it worked out?

A. He and his wife signed the mortgage.

Q. To himself? [34]

A. Well, there were other signers with him, there were other signers on the mortgage, instead of making a separate mortgage they all signed on the same mortgage.

Q. Now, why did you include that terminal?

A. It was included as additional security.

Q. Did Markee owe you any money on that terminal prior to that time?      A. I think not.

Q. Did you ever have a mortgage to the terminal?

A. No, I never had a mortgage on it. Mrs. Haas at Sheridan had a mortgage.

Q. Did you pay that mortgage off for Mr. Markee?

A. No, I think Mr. Markee paid it off himself.

Q. Was it paid off before or after this second mortgage was executed?

(Testimony of Otto W. Heider.)

A. Now, as to date of payment—Mrs. Haas advanced the money to Mr. Markee to build it personally. I know about the transaction, but I can't tell you what date it was paid off, whether it was before or after, but I think he paid it off by the month.

The Referee: We will recess for five minutes.

(Short recess.)

Q. (By Mr. Bollenbeck): Now, Mr. Heider, you stated that you had never had anything to do with the business affairs of the Rand Truck Line, is that right? [35]

A. Oh, I never was their attorney. They had attorneys here in Portland. I don't know who they were, but they had, I think had, attorneys on a retainer by the year.

Q. Did you ever have their minute book, keep the minute book or by-laws in your possession?

A. Oh, I did some notary work for them, some odd jobs.

Q. I am not talking about notary work, I am talking about keeping the corporation records.

A. Oh, I never kept the corporate records.

Q. Never kept the corporate records?

A. No.

(Letter to Rand Truck Line by Otto W. Heider dated November 28, 1947, so produced, was thereupon marked Trustee's Exhibit 5.)

(Testimony of Otto W. Heider.)

Q. (By Mr. Bollenbeck): May I hand you Trustee's Exhibit 5 and ask if that is your signature?

A. I never kept them, I just sent these to Rand Truck Line.

Q. Just answer the question. Is that your signature?

A. Yes, that is my signature, but I never made up the by-laws or corporate records.

Q. How did you happen to have a copy of the by-laws?

A. I think they were left there by Mr. Rand for safekeeping, that is how I happened to have them. I never made them up at all.

Q. You mean this is a copy of the by-laws Mr. Rand left in [36] your office?

A. Just with some other old books and seal and other old books of the company, left them there temporarily.

Q. How did you happen to have the seal?

A. Well, I think he had it there at the time he put the seal on the mortgage.

Q. And left it there?

A. Left it there for awhile. I think they subsequently came and got it, but I never had charge of those things, just temporarily, just a temporary arrangement.

Q. How temporary, how long were they there?

A. He came back to town once a month when he was closing up his accounts with the different shippers and things and he would stop in and sometimes he would pick up one thing and sometimes another.

(Testimony of Otto W. Heider.)

Q. But he didn't pick up the by-laws?

A. I think that was an unsigned copy of the by-laws. I don't think—I am not sure. Mr. Taylor should have them. I never did write the by-laws for Rand Truck Line.

The Referee: Or the minutes of any of their meetings?

A. No, they usually had someone keep the minutes of their meetings. We might have typed them up in our office.

Q. (By Mr. Bollenbeck): Well, who dictated them?

A. I don't know who dictated them. I didn't dictate them.

Q. You never dictated any of the corporate minutes? [37]

A. I never kept the corporate records at all or prepared any of them.

Q. Just answer the question. Did you ever dictate any of the corporate minutes?

A. Well, I might have dictated on one or two occasions a small portion of the corporate minutes.

Q. Those occasions might be the occasions when these mortgages were given, mightn't they?

A. I don't know about that.

Q. You would be vitally interested in that part of the corporate minutes, wouldn't you, Mr. Heider?

A. Oh, I don't know necessarily why.

Q. Just answer the question. Would you or wouldn't you?

(Testimony of Otto W. Heider.)

A. Well, no. I had ample security. I had ample collateral all the time.

Q. Do you have the certificates of title of the motor vehicles there? A. Yes.

Q. May I see them, please. Do you have the ICC and PUC certificates?

A. Oh, no, I don't have them, never did have them.

Q. Now, there is one thing I can't understand about these mortgages, Mr. Heider, this Vern Markee mortgage, the original mortgage of \$5400 payable to the Rand Truck Line.

A. That was taken up by the second [38] mortgage.

Q. Well, now, let's get to that step by degrees.

A. All right.

Q. They executed—rather, Vern Markee gave the Rand Truck Line this mortgage dated October 31, 1945, on a Sterling truck, is that right?

A. Well, the description states there—

Q. One Sterling truck, model engine 44. Now, what happened to that mortgage then as far as you know? A. Why, it was filed, I suppose.

Q. Well, I mean did the Rand Truck Lines sell it to you?

A. I think that they sold it to me along with their other security.

Q. Well, when we were talking about this awhile back you stated that they had sold it to you, if I remember rightly. A. The Rand Truck Line?

Q. Yes. A. Had assigned it to me.

(Testimony of Otto W. Heider.)

Q. Well, they assigned it to you? A. Yes.

Q. And at that time you didn't know how much you had paid for it?

A. Oh, I told you I thought it was \$5100—I can't tell exactly. It was \$5100, between \$5100 and \$5200, and some cash.

Q. How much?

A. I'd say between \$5100 and \$5200. [39]

Q. And you stated you couldn't find the cancelled check?

A. I didn't find it yesterday when I was going through.

Q. Now, did you find the checks for the month of November, 1945? A. For what?

Q. For the month of November, 1945.

A. On what transaction?

Q. Well, your checks for November.

A. For what—oh, the checks to Rand—you have them in your hand.

Q. Well, there are some of those checks issued during the same month that this transaction occurred. Now, how did you happen to find these checks and not the check involved in this transaction?

A. I think probably with additional search I can probably find the checks.

Q. Do you keep your checks for one month together? A. No, I don't.

Q. What kind of a filing system do you have?

A. We usually keep them for two or three months together.



(Testimony of Otto W. Heider.)

Q. All right, you keep them for two or three months together and you found that particular batch of checks because you delivered the Rand checks. Why is it you couldn't find this check?

A. Why, I probably could find the checks. [40]

Q. Did you make an effort to find them?

A. Yes, I made an effort to find them and probably could find them.

The Referee: Well, without going into that detail, why, we will ask that if he can produce the check by which he purchased the Vern Markee mortgage——

A. Yes, I have a notation of date there and I can make another search, if the Court please.

Q. (By Mr. Bollenbeck): Also the Earl Walden mortgage, and if he can't find the checks, to produce the bank statements.

A. The bank statements wouldn't show the names of the payees.

The Referee: Well, still on this particular mortgage, you bought it from Rand Truck Line. Rand Truck Company didn't owe you any money on that?

A. You mean the first mortgage?

The Referee: No. I am talking about this Vern Markee mortgage.

A. Oh, yes—oh, this last mortgage.

The Referee: The Vern Markee mortgage.

A. They didn't owe me anything on that. I just paid them cash out on that.

The Referee: Yes, but then when you made this

(Testimony of Otto W. Heider.)

refinancing, why, you charged the Rand Truck Company for the balance due on that mortgage, \$2550.

A. Yes. [41]

The Referee: Well, did they owe you that?

A. Yes, they did.

The Referee: I thought Vern Markee would owe it to you.

A. Well, it is Rand—let me see the mortgage. Well, it was all in the same transaction. It was all taken up. This mortgage was given by Vern Markee, was given for the benefit—it was made out to the Rand Truck Line and made for the benefit of the Rand Truck Line. They got the proceeds out of the mortgage.

The Referee: And then you bought it from the Rand Truck Line?

A. Yes, I bought it from the Rand Truck Line.

The Referee: And did they endorse it without recourse?

A. No, they endorsed it with recourse.

The Referee: So you looked to them for the repayment of that mortgage?

A. Not now, because it was taken up.

The Referee: But at that time? A. Yes.

The Referee: And who was paying for that?

A. Who was making the payments?

The Referee: Yes.

A. The Rand Truck Line.

The Referee: Even though it was executed by Vern Markee to the Rand Truck? [42]

A. Yes, because he was one of the principal offi-

(Testimony of Otto W. Heider.)

cers of the Rand Truck Line and the money that was represented by this mortgage went for the benefit and use of the Rand Truck Line, that is right.

The Referee: The Rand Truck Line was operating this piece of equipment? A. Yes, it was.

The Referee: Not Vern Markee?

A. Well, Vern Markee was one of the operators of it for the Rand Truck Line, that is right, but the money represented by the mortgage went into the Rand Truck Line, to the benefit of the Rand Truck Line.

Q. (By Mr. Bollenbeck): Now, Mr. Heider, did you state this first mortgage was prepared in your office? A. Yes, I think it substantially was.

Q. I mean, it was typed in your office?

A. Yes, it was typed in my office and then checked by Rand.

Q. Now, do you know whether the minutes of the meeting authorizing this particular mortgage were typed in your office?

A. Let me see the minutes. I can't tell.

Q. The minutes of September 28, 1944, referring particularly to the second page thereof where it says "It is moved and seconded that the President and Secretary of the Rand Truck Line, Inc., together with the Vice President, borrow from Callie B. Heider on assignment from Mrs. R. R. Rand the sum of \$43,560." [43] Now, was that prepared in your office?

A. Well, that is the 28th day of September, '44. That is the first one. I can't say whether that was

(Testimony of Otto W. Heider.)

prepared in my office or whether Mr. Rand brought this to my office, but I am sure I have seen these minutes before.

Q. The minutes of the meeting authorizing the execution of this mortgage provided it was to be, the money was to be borrowed from Callie B. Heider. Now, who is Callie B. Heider?

A. That is my wife.

Q. That is your wife?           A. Yes.

Q. You are unable to state at this time——

A. Well, I am not sure whether they prepared them and brought them to my office, but I have seen the minutes.

The Referee: You saw them at that time?

A. Yes, or I am sure shortly after they were prepared I saw them.

The Referee: Mr. Bollenbeck, the record would be more complete if you would introduce the first mortgage into evidence as an exhibit. It is not in.

A. And the minutes, too. I would like to see them introduced to complete the record.

(Mortgage by Rand Truck Lines, Inc., to Mrs. R. R. Rand, dated September 28, 1944, and accompanying papers, so produced, was thereupon marked [44] Trustee's Exhibit 6.)

The Referee: And Mr. Heider asked that the minutes be introduced.

(Document entitled on the first page "By-Laws of Article I" so produced, was thereupon marked Trustee's Exhibit 7.)

(Testimony of Otto W. Heider.)

The Referee: I notice the minutes are not bound in a book. Wasn't there a book that these minutes were bound in?

A. Not unless Mr. Taylor has a book.

Mr. Bollenbeck: As a matter of fact, your Honor, they weren't even stapled together until I stapled them. They were just loose.

The Referee: In whose possession were these minutes at the time of filing the bankruptcy?

Mr. Taylor: I had them in the office, your Honor.

Mr. Bollenbeck: In the office of Mr. Taylor.

Mr. Tonkon: He delivered them to me immediately prior to the filing of the petition and I turned them over to the Trustee's counsel.

Q. (By Mr. Bollenbeck): Now, Mr. Heider, weren't you vitally interested in having a proper resolution drawn by the corporation to authorize the execution of these mortgages?

A. I think that is a good idea. I have no objection to it.

Q. As a matter of fact, it is essential, isn't it?

A. Well, not necessarily, not necessarily, where you are [45] holding the stock of the corporation and showing the legal owner on the title, it isn't necessary.

Q. And you mean you didn't show any interest whatsoever in what the minutes of the corporation showed?

A. Oh, yes, I think that is very essential.

Q. And as a matter of fact you prepared them, didn't you?

(Testimony of Otto W. Heider.)

A. I may have checked them but I don't know whether they were prepared, whether Mr. Rand's attorney prepared them or whether I prepared them. I may have prepared them.

Q. Well, have you compared the typewriting of those minutes of that meeting and the original mortgage?

A. Well, I have five typewriters in my office and——

Q. Well, it is fortunate that these were prepared on the same one, then, isn't it?

A. Were they prepared on the same typewriter? That is the one.

Q. Now, this original first mortgage was prepared in your office?      A. Yes.

Q. And the minutes seem to be prepared on the same typewriter.

A. They very likely were, then.

Mr. Tonkon: Will you qualify the minutes?

Q. (By Mr. Bollenbeck): Minutes of the meeting of September 28, 1944.

A. They were likely written in my office. The typewriting looks familiar. [46]

Q. And it looks identical, does it not?

A. Yes, quite familiar. They are not identical because I think they are probably on different typewriters, but on Royal, different typewriters.

Q. Now, Mr. Heider, these checks indicate that you paid this money to Rand at the rate of \$500 a month—\$500 a week, rather.

A. Yes, I think that is better.

(Testimony of Otto W. Heider.)

Q. Why was that done?

A. I didn't have the money.

Q. You were unable to pay the full amount right at that time?      A. That is right.

Q. However, your mortgage as prepared, you were collecting interest on the full amount for the full period of time?

A. Yes, but I settled with Rand on the interest too, I paid Rand interest.

Q. You paid Rand interest?

A. Yes, I did.

Q. What rate did you pay Rand that?

A. Oh, I think I paid him 8 per cent.

Q. Did you have a written agreement with him on that?

A. I think I had a collateral agreement with him, because he didn't pay it—didn't turn the stock of the company over until I settled with him in full. I have the stock here now. You haven't asked for [47] it.

Q. Mr. Heider, I thought I had the stock.

A. Do you have the stock? Maybe we have two sets of stock, then. That is okeh. I guess we got two sets of stock.

The Referee: Do you have checks to show the interest that you paid to Rand?

A. I think they are in there, I think most of them are in there. That was a private matter between Mr. Rand and myself because I didn't have the money to pay him at the time.

Q. (By Mr. Bollenbeck): Now, these payments

(Testimony of Otto W. Heider.)

on this first mortgage that you have shown here as Trustee's Exhibit 1, how were those payments received?      A. By check.

Q. All of them by check?

A. Oh, I think so.

Q. And did you at any time get cash?

A. I think they came through the mail from Rand Truck Line.

Q. Did you ever get cash any time?

A. Oh, probably did, but most of the time it was by check.

Q. Who paid the payments to you?

A. Oh, some representative of the Rand Truck Line.

Q. Who would they be?

A. Oh, Mr. Taylor, Mr——

Q. We are talking about the first mortgage now. Mr. Taylor wasn't with the company now at the time of the first mortgage.

A. Well, the first mortgage—well, I think maybe Mr. Markee, [48] the principal officer.

Q. Which Mr. Markee?

A. Well, it might have been in some cases Loren Markee, but the most of the time I think it was Vern Markee.

Q. And did they pay in cash?

A. Did they pay in cash?

Q. Yes.

A. Sometimes they paid in cash but most of the times they paid in check.



(Testimony of Otto W. Heider.)

Q. Most of the time they paid by cash?

A. It might be so. And sometimes it was paid by check and I would give receipts too.

Q. And on your receipts you would specify it was by check or cash? A. Oh, not always.

Q. Not always? A. Not always.

Q. Mr. Heider, I am going to refer——

(Sheaf of receipts, so produced, was thereupon marked Trustee's Exhibit 8.)

Q. (By Mr. Bollenbeck): I am going to refer you to Trustee's Exhibit 1 and the payment of September 15, 1945, in the amount of \$1000 and hand you Trustee's Exhibit 8, dated September 14, 1945, in the amount of \$1,050 and ask you why the discrepancy?

A. Well, there is probably some other item they owed me on [49] at the same time. That is probably—they are credited with \$1000, but there is probably some other item.

Q. What other item would it be?

A. That is four years ago. I couldn't tell you at the moment, but probably there is some other item.

Q. Do your records show what other item it was?

A. I don't have a record, but that might have been by check and by cash both. This may have been by check and by cash both, so I couldn't tell you.

Mr. Bollenbeck: As far as we are marking things by lot I would also like to include the rest of these exhibits with the one of September 14th so I can refer to them.

The Referee: All the receipts produced by Mr.

(Testimony of Otto W. Heider.)

Heider on the first mortgage may be included in Trustee's Exhibit 8.

Q. (By Mr. Bollenbeck): Now, on October 1st, 1945, you have got \$1000 there, and I hand you a receipt for \$1050.

A. That was on—I think there was some \$50, that it was on some services that I rendered.

Q. Now, what services? A. To whom?

Q. To whom?

A. Some services I rendered along about that same time or prior.

Q. To whom?

A. Well, it was to the Markees for operating the Rand Truck Line. [50]

Q. What kind of services would those be, Mr. Heider? A. Oh, legal services.

A. Oh, I thought you said you were never their lawyer?

A. I said the Rand Truck Line, for Bob Rand, while Bob Rand had it I was never attorney for Bob Rand.

Q. Oh, you were attorney for Rand Truck Line after Markee's took over?

A. Oh, I did some services after Markee took over, not for Rand.

Q. And you did prepare these mortgages, both of them?

A. Oh, they were prepared in my office.

Q. And you did prepare the corporation minutes? A. Oh, I don't know about that.

Q. What would they be paying you \$50 for?

(Testimony of Otto W. Heider.)

A. Legal services.

Q. What kind of services?

A. Various kinds.

Q. Let's be specific.

A. Some paper, document—they might come in with something to the Public Utilities Commissioner or something. It might be various legal services.

Q. Did you act for them before the Public Utilities Commissioner?

A. No, I never appeared before the Public Utilities Commissioner.

The Referee: Did you render some statement to them that you might have copies of? [51]

A. No, I didn't render statements to them that I recall, but I might find statements of it, though. That was four years ago and I might possibly go back and find the statements.

Q. (By Mr. Bollenbeck): Now, I am going to refer you, Mr. Heider, to a receipt issued to Vern Markee on January 11, 1946, in the amount of \$450.

A. I think that was on that mortgage over there.

Q. Do you know whether that was paid in cash and check?

A. Well, it might have been paid both ways, cash and check.

Q. You did get cash quite a bit of the time?

A. Oh, yes, and I paid out cash too.

Q. In other words, your statement when you first started talking about cash and checks is not quite correct?

(Testimony of Otto W. Heider.)

A. It is cash and checks both. I think sometimes they give me a check on that and part cash.

Q. And that happened a good many times, did it?

A. Well, a number of times.

Q. That you received cash and check?

A. Yes.

Q. Do you know any reason why it would take place that way?

A. Now, why they wanted to pay their debts that way I don't know. They probably had the money available and wanted to pay it that way is all I can tell you.

Q. Now, you, of course, filed your income tax return for '44, '45, '46, and '47? [52]

A. Yes.

Q. And in making those income tax returns did you make the proper entries for interest collected and interest paid?

A. Oh, yes.

Q. And will you produce those income tax returns here?

A. I haven't got them.

Q. You haven't got them?

A. With me, no.

Q. Do you have them available in Sheridan?

A. I don't know whether I have them available or not. I think that I have copies available.

Q. Will you produce the copies?

A. Well, I don't have them here.

Q. Will you produce them at a time to be fixed by the Court?

A. I could produce them.

Mr. Bollenbeck: I would like to ask the Court for an order.

(Testimony of Otto W. Heider.)

Q. Will those income tax returns show these particular items? A. No, they won't.

Q. Do you have any documents or records showing these particular items?

A. Well, on that \$50 item I think I can find maybe a statement or something for that.

Q. And how about the interest earned and interest paid on these mortgages and paid to Rand?

A. You have cancelled checks. [53]

The Referee: How do you keep books to determine what interest is earned?

A. I keep a separate set of books for that.

The Referee: You have a separate set of books?

A. Yes, I have.

The Referee: And you make those entries of these payments? A. Yes, that is right.

Q. (By Mr. Bollenbeck): Mr. Heider, didn't the Court order you to produce the original books today? A. I produced the books.

Q. I am talking about the books.

A. You have it over there.

Q. You have now told the judge you have a set of books.

A. He was asking about income tax returns.

Q. You have to enter these items.

A. I don't have to enter who pays them, where they come from, that way. I just enter that much.

Q. You do have a ledger sheet on this transaction?

A. No. You have the sheet on the transaction right there. I give it to you awhile ago.

(Testimony of Otto W. Heider.)

Q. From what books and records do you determine your income tax?

A. Well, I have a separate set of books showing my income and disbursements.

Q. Has that got a sheet for this transaction? [54]

A. Not a particular sheet for that. I enter it up just as the thing accrues.

Q. Do these records show to whom you paid the money and from whom you received it?

A. Not to whom, it doesn't show that. That isn't required.

Q. All it shows is receipts and disbursements?

A. What?

Q. All it shows is receipts and disbursements?

A. Receipts and disbursements.

Q. No names? A. No names.

Q. No transactions identified?

A. No transactions like this would be set up like that.

Q. Have your books ever been checked by the Internal Revenue Department?

A. Oh, they are checked every year.

Q. And they approve that kind of books and records?

A. Well, they set them up for me and they are checked every year, have been for years.

Mr. Bollenbeck: I would like to ask the Court for an order requiring Mr. Heider to produce his books and records. His testimony is very unsatisfactory, and I trust that the books and records will be

(Testimony of Otto W. Heider.)

more satisfactory. I'd also like a copy of his tax returns.

A. You have all the books and records that I have got. [55]

The Referee: He stated those books will not show anything on these transactions.

A. Show absolutely nothing.

The Referee: I will not make such an order at this time. Now, has he produced the receipts on the second mortgage showing what the balance is? What is that item?

A. On the first mortgage?

Q. (By Mr. Bollenbeck): I haven't got to the second mortgage yet.

A. Let's see, I thought I had given it to you. No, here it is on the second mortgage. Here is the assignment too. You didn't ask for that, Mr. Bollenbeck.

Q. You have, I take it, in your claim on the second mortgage demanded the entire amount at this time?

A. You called me up, Mr. Bollenbeck, and said you wanted to pay it off, and I told you the amount.

Q. What did you tell me at that time?

A. I told you I would give you a discount.

Q. How big a discount?

A. I don't remember now whether it was 3 or 4 per cent.

Q. Well, in your claim that you filed in here you have accelerated the mortgage and claimed the entire amount.

A. The mortgage accelerates itself.

(Testimony of Otto W. Heider.)

Q. In other words, it is your position that the mortgage has accelerated? [56]

A. There is a breach in it.

Q. And the entire amount is due and owing?

A. That is according to the terms of the mortgage.

Q. And that is according to your understanding of it? A. That is the way it reads.

The Referee: His proof of claim states that.

Q. (By Mr. Bollenbeck): I notice, Mr. Heider, there are some payments that you say "Received from R. J. Werner." Who is R. J. Werner?

A. Oh, that is a truck that Mr. Taylor sold that was taken out of the mortgage and it was leased to Mr. Werner and he made some payments on it.

Q. He paid them direct to you, did he?

A. Yes.

Q. And it was applied on the mortgage?

A. They were applied on the mortgage. It was a Sterling truck, I believe, a single axle.

The Referee: Do you want to introduce that statement into evidence?

A. If the Court please, are those certificates of title introduced in evidence?

The Referee: No, they are not.

(Tabulation with beginning date 11-2-48 and closing date of 5-10-49 and accompanying payers, so produced, was thereupon marked Trustee's Exhibit 9.) [57]

Q. (By Mr. Bollenbeck): Now, Mr. Heider, who



(Testimony of Otto W. Heider.)

at the Internal Revenue Department set up your books?

A. Oh, I can't tell you. About ten years ago they showed me the system to use, and that is the system I have been using ever since.

Q. Do you have any objection to this court selling this equipment free from the lien of your mortgage with the amount and validity of your mortgage to be determined in the future by this Court?

A. I asked you on the phone, Mr. Bollenbeck, if you had a buyer of it and instead of giving me a civil answer you gave me anything but one, so I don't know what you have in mind.

Q. Just answer my questions.

A. No, I wouldn't want to handicap the Company if they had a buyer, a cash buyer, and then the amount could be determined. I wouldn't have any objection to it if they had an immediate cash buyer and wanted to make a sale if it would expedite matters or be of any advantage to the corporation. I wouldn't have any objection.

Q. You would have no objection to do that then? Well, that being the case would you be willing to surrender the title policies to the Trustee in Bankruptcy?

A. Whatever Referee Snedecor says in that regard I will be very glad to comply with his request.

The Referee: Mr. Heider, it is the practice of this Court [58] to sell property free from liens, the order providing that the proceeds shall be impressed with all valid liens as determined by the Court.

A. That is satisfactory.

(Testimony of Otto W. Heider.)

The Referee: And if an order is so made it would provide that the proceeds shall be held in lieu of the property itself.

A. That is right.

The Referee: To be impressed with any valid liens and the money paid on those liens by order of the Court.

A. That is okeh, satisfactory with me.

Mr. Tonkon: Of course, subject to the further determination of the Court as to the validity of the liens.

The Referee: Validity and amount of the liens, amount owing.

Mr. Bollenbeck: In this particular case, your Honor, because of the unusual circumstances I would like to keep the mortgage alive in favor of the Trustee in Bankruptcy. I don't just exactly know how it is going to be done yet.

Mr. Tonkon: How do you mean "yet"?

Mr. Bollenbeck: Without being cancelled.

The Referee: Well, selling the equipment doesn't satisfy the mortgage. The mortgage is still there and the proceeds are held in lieu of the mortgaged property. That is a matter that you might determine by the order. Mr. Heider has the assignment of this second mortgage. Perhaps that should go [59] in evidence.

Mr. Bollenbeck: Yes.

(Assignment of mortgage and note dated August 7, 1946, so produced, was thereupon marked Trustee's Exhibit 10.)

(Testimony of Otto W. Heider.)

The Referee: It will be understood that if a satisfactory sale is made that Mr. Heider will then present the certificates of title endorsed so that the assets may be transferred without delay to the purchaser. A. That is very satisfactory.

Mr. Tonkon: I think the order should also include some papers or documents in connection with the Rand Truck Line.

A. If the Court please, if it will be of any assistance to Mr. Bollenbeck about maintaining the mortgage, I can make an assignment of the mortgage to the Trustee if it will be of any assistance.

The Referee: Well, that will be a matter of future determination. Now, Mr. Heider, do you have in your possession any original documents that belong to the Rand Truck Line, the Bankrupt?

A. Well, these certificates of stock here.

The Referee: You have certificates of stock? I think you gentlemen might, without encumbering the record, check those between yourselves afterwards while you are still here. Do you have any original corporate minutes? [60]

A. No, I don't have any at all. Those are all.

The Referee: The reason I ask you that question is that I notice that the corporate minutes authorizing that first mortgage seem to be the carbon copies. A. That is the original.

The Referee: Well, I saw one carbon copy.

Mr. Bollenbeck: They have copies in there too, your Honor.

The Referee: I see. Well, then, the order of the

(Testimony of Otto W. Heider.)

Court will be that the property may be sold free from lien, including in the order the safeguards which have already been mentioned, and the Court will not at this time pass on the question of the amount owing or any questions that might be raised as to the validity of the mortgage. Those are questions that Mr. Heider will have ample opportunity to meet at the time, but it is hoped, Mr. Heider, that we can sell this truck line, the equipment, as a going concern in order to get some value out of the permits, and it would be to the advantage of all. We expect to sell it for considerably more than the amount you claim and the matter of determining the validity and amount of your lien will be taken up and if the Trustees have any objections to it you will be served with the objections and then there will be a further hearing on it. I am not determining that matter at all. Is that all now?

Mr. Bollenbeck: I have Vern Markee here.

The Referee: Well, it is noon now. He was subpoenaed? [61]

Mr. Bollenbeck: Yes, your Honor. I take it the gentlemen will still be under subpoena for the rest of the day?

The Referee: Yes. Was Mrs. Markee subpoenaed?

Mr. Bollenbeck: No, she wasn't.

The Referee: We will take up again at 2:00 o'clock.

(Witness excused.)

(Noon recess.) [62]

Afternoon Session—2:30 P.M.

The Referee: Now, Mr. Vern Markee, will you come up, please.

VERN MARKEE

was thereupon produced as a witness in behalf of the Trustee and, being first duly sworn, was examined and testified as follows:

Direct Examination

By Mr. Bollenbeck:

Q. You are Mr. Vern Markee?

A. Yes.

Q. And Florence Markee is your wife?

A. That is right.

Q. When did you first become connected with the Rand Truck Line?

A. In about September of 1943.

Q. And how did you become connected with the Rand Truck Line?

A. My operation was consolidated and I went in as a partner with Bob Rand.

Q. Well, you bought some stock in the Rand Truck Line, didn't you?      A. That is right.

Q. You bought 250 shares of stock and your wife Florence Markee took 250 shares of stock?

A. Yes.

Q. And what did you pay for that stock? [63]

A. There wasn't any cash involved. It was a transfer of equipment.

(Testimony of Vern Markee.)

(Carbon copy of document dated December 27, 1943, so produced, was thereupon marked Trustee's Exhibit 11.)

Q. (By Mr. Bollenbeck): I hand you Trustee's Exhibit 11 for identification which purports to be a bill of sale signed by yourself and Florence Markee transferring certain equipment to the Rand Truck Line. Is that the equipment that you turned over to Rand in return for these 500 shares of stock?

A. Yes, it is.

Q. And this bill of sale was delivered at that time?

A. Yes, sir.

Q. Now, this specifically covers "all permits of the Public Utilities Commission of the State of Oregon and the United States Interstate Commerce Commission for the operation of the above-described trucks as a common carrier." Now, what permits did you have at that time, Mr. Markee?

A. I had a Public Utility Commission permit, anywhere for hire permit within, from and to sixty road miles radius of Sheridan.

Q. Is that the only permit you had?

A. No, that was the Public Utilities Commissioner permit.

Q. What other permits did you have?

A. I had an Interstate Commerce permit which was authority to haul interstate commerce freight between Portland and Sheridan. [64]

Q. Were those the only permits you had?

A. That is right.

(Testimony of Vern Markee.)

Q. And those were the permits that were transferred to the Rand Truck Line?

A. No. One of those permits was cancelled and the other was never transferred.

Q. Which one was cancelled?

A. The Interstate Commerce permit.

Q. The Public Utilities Commissioner permit was never transferred?

A. That is right.

Q. Now, you are operating down there in Sheridan now, aren't you?

A. That is right.

Q. And what kind of an operation do you have?

A. We have an anywhere for hire operation within, from and to a sixty road mile radius of Sheridan.

Q. Are you using the permit that is covered under this bill of sale?

A. Yes.

Q. And you are operating in competition with the Rand Truck Line?

A. Yes.

Q. On a permit that you give a bill of sale to?

A. The permit was never transferred.

Q. Well, now, you give a bill of sale to it, didn't you?

A. That is right. [65]

Q. Why wasn't it transferred?

A. Because it didn't have the authority of the Public Utility Commission.

Q. Did you ever apply for that authority to transfer it?

A. No, sir.

Q. And you were an officer of the corporation at that time?

A. Yes.

Q. There is a suit pending now by the Rand Truck Line against you, is there not, involving this

(Testimony of Vern Markee.)

same permit? A. Yes.

Q. What excuse do you have for continuing operation under a permit that belongs to the Rand Truck Line?

A. The permit doesn't belong to Rand Truck Line.

Q. Well, it doesn't belong to it merely because you yourself failed to have it transferred, doesn't it?

A. No. The permit—when I went in with Rand, why, the permit was not transferred because at any time if I wanted to I could reinstate the permit. The permit was froze for the duration of the war.

Q. Wait a minute—that you could reinstate the permit? A. Yes.

Q. As your own property?

A. I froze the permit. The permit has always been in mine and my wife's name.

Q. But you transferred it to the Rand Truck Line by this bill [66] of sale.

A. No. It was never transferred.

The Referee: You agreed to transfer it, you mean?

A. Yes.

The Referee: Did you get the 500 shares of stock?

A. I got 250 and my wife got 250.

The Referee: That was full consideration?

A. Yes.

Q. (By Mr. Bollenbeck): Since you agreed to transfer this permit to the Rand Truck Line are



(Testimony of Vern Markee.)

you willing to abide by your agreement and transfer it.

A. Well, the agreement with Bob Rand was subject to the fact that if I wanted to resume operation that it could be, that the permit was still mine; in other words, there was no consideration for the permit in the first place. The Public Utilities Commission will not let you transfer the permit without a hearing and it was not the intent.

Q. Is there anything in writing that says that?

A. Yes.

Q. What?

A. An agreement between Bob Rand and myself.

Q. Let's see it.

A. I don't have it with me.

Q. Can you produce it? A. Yes. [67]

Mr. Bollenbeck: I would like to ask the Court for an order requiring him to produce it.

The Referee: You will be asked to produce that at a future hearing and we will fix a time for it.

Q. (By Mr. Bollenbeck): Now, subsequent to that time, Mr. Markee, did you purchase any additional stock in the Rand Truck Line?

A. Yes.

Q. Well, when did you buy some additional stock and from whom did you purchase it?

A. From Bob Rand in 1945, I believe.

Q. And how many shares of stock did you buy then? A. I don't remember.

Q. Well, I will refresh your memory. Did you buy 2,000 shares and Loren Markee buy 2,000 shares? A. I believe that is right.

(Testimony of Vern Markee.)

Q. 4,000 shares. And how did you pay for that stock? A. We didn't.

Q. We didn't? A. No.

Q. Well, just what was the transaction?

A. We signed a mortgage with Otto Heider.

Q. This mortgage was \$43,560, I think. How much did you agree to pay for this stock?

A. That I don't know.

Q. Well, you certainly must know how much you were going to [68] pay.

A. Well, it was for the balance of the stock we was buying at par value from Bob Rand, outstanding stock that my wife and I did not have.

Q. That was 4,000 shares?

A. That is right.

Q. Now, who acted as your lawyer in that transaction? A. I don't believe we had a lawyer.

Q. Was Mr. Heider involved in the transaction?

A. Mr. Heider was there, yes.

Q. Was he there before the deal was made?

A. No.

Q. Well, now, how did you—what was the first document you signed between yourself and Rand involving the sale of this stock?

A. I believe it was an agreement. I am not sure. It's been a long time.

Q. An agreement to buy at par? A. Yes.

Q. Would that be \$40,000, 4,000 shares at \$10 a share? A. Yes, I believe that is right.

Q. Well, now, do you know, Mr. Markee, or don't you?

(Testimony of Vern Markee.)

A. I am not sure. It's been a long time ago. You have got all the stuff there.

Q. No, I haven't got that. You heard Mr. Heider's testimony [69] this morning that he paid the Rands about \$36,000. A. Yes.

Q. Is that what the purchase price of the stock was?

A. The purchase price of the stock was what remained of the issued stock that we did not have.

Q. Well, how much were you going to pay for that? A. Par value, whatever it was.

Q. Well, par value I think would be \$40,000, but you didn't pay \$40,000 for it.

A. What did we pay for it?

Q. Did you pay any money to the Rands other than the money that Mr. Heider paid them?

A. No, we didn't.

Q. You didn't. Did Loren Markee put up any money at the time? A. Yes.

Q. In addition to the money that Mr. Heider paid? A. Yes. That wasn't paid to Rand.

Q. Where did that money go?

A. I don't know.

Q. What do you mean you don't know?

A. It is like I said, it's been a long time ago. It's all down there in the record.

Q. The money that Loren Markee paid, did it go into the corporation?

A. The money he put in went in for stock. I am sure it didn't [70] go for the corporation.

Q. To whom did it go, to you? A. No.

(Testimony of Vern Markee.)

Q. Did it go to Mr. Heider?

A. No. I believe it went to Rand. I am not sure.

The Referee: Do you remember how much it was? A. \$5,000.

The Referee: \$5,000. That was in cash?

A. Yes.

Q. (By Mr. Bollenbeck): In other words, now the transaction is that Loren Markee paid \$5,000 to the Rands and Mr. Heider paid approximately \$36,500 to the Rands and for that you and Loren equally got 4,000 shares of capital stock in the Rand Truck Line, is that right?

A. Got 4,000 or 2,000?

Q. You got 2,000 each?

A. That is right.

Q. And I understand you did not put up any cash. A. No. I put up my equipment.

Q. Well, I mean that equipment was for that 500 shares that you had originally purchased.

A. That is right.

Q. But for the additional 2,000 shares that you purchased you did not put up any money?

A. No. [71]

Q. Now, when did Mr. Macy come into the corporation? A. About 1946.

Q. And how did he come in, I mean did you and Loren sell him some stock? A. Yes.

Q. And how many shares did you sell him?

A. I don't recall. We split it three ways again, split it three ways instead of two ways.

Q. And what consideration did he pay?

(Testimony of Vern Markee.)

A. \$5,000.

Q. To whom did he pay it.

A. My brother and I.

Q. Now, how did Mr. Taylor come into the picture? Did he buy stock or was that stock given to him?

A. That stock was given to him.

Q. The stock was given to him. Now, getting back to this first mortgage that the Rand Truck Line gave——

A. May I clear up one item, your honor? That \$5,000 that Mr. Macy put in was turned over to Mr. Heider on the mortgage.

Q. (By Mr. Bollenbeck): Who made the payments to Otto Heider on this first mortgage?

A. Oh, I made some of them myself, some of them were mailed in, Gordon Mize in Portland made some of them.

Q. Were they made in cash or by check?

A. Both. [72]

Q. Where did the cash come from?

A. Came out of the company.

Q. And did the checks come from the company too?

A. Yes.

Q. When those payments were made to Mr. Heider how were they entered in the books, do you know?

A. No, I don't.

Q. Isn't it a fact that they were first entered as an account receivable from officers, isn't that the way you first entered them in the books?

A. I never entered them myself. I didn't take care of the bookkeeping.

(Testimony of Vern Markee.)

Q. Well, you supervised the bookkeeping, did you not?      A. No. I was there.

The Referee: Who was your bookkeeper?

A. Allan Brigg, Portland, the office manager. He took care of the books.

Q. (By Mr. Bollenbeck): Now, Mr. Markee, I am going to hand you here Trustee's Exhibit 1 for identification and I am going to also hand you here an analysis of your other investment officers account. Can you tell me why Mr. Heider should show that \$1,000 payment was received and why on the same date a charge should be made against the officers, say on December 28, 1944? Otto Heider shows a credit on the mortgage of \$1,000 and you show that you have charged the officers account \$520.57. [73] Can you tell me why that discrepancy?

A. I have no knowledge of this at all. I can't say.

Q. Well, let's take the statement of March 30th, 1945. Your account officers shows a charge against you and payment to Otto Heider of \$463.26. Otto Heider shows a credit on the mortgage of April 2nd of '45 of \$1,000. Now, I have here your original accounts receivable for 1945—strike that. Well, I am going to have to change my question here because of the books. You show, Mr. Heider shows on April 2nd, 1945 a credit of \$1,000. Now, on March 9th, 1945 you paid R. R. Rand, or rather there was charged to your officers account on account of a payment to R. R. Rand, of \$472.93, and on March

(Testimony of Vern Markee.)

30th Otto Heider \$463.26. I see an entry here in your accounts receivable which is \$496.19, being the total of those two checks or those two charges against your account to Rand and Heider. Now, where did the difference between this \$463.26, which was charged to your account and paid to Heider, and the \$1,000 which he shows as a credit come from?

A. It came from out of the company as far as I know.

Q. You mean there was income from the company that didn't go through the books?

A. If it doesn't show it on there. I didn't keep those books. I am not sure what there is in there. You seem to have some trouble figuring them out yourself. I don't see how you expect me—I am not an accountant. [74]

Q. Was there income from the use of the company equipment that did not go through the books of the Rand Truck Line?

A. Yes.

Q. And where was that money paid?

A. It was paid to Otto Heider.

Q. Now, was that a consistent practice of the Rand Truck Line at that time?

A. That didn't happen very often.

Q. How often did it happen?

A. That I can't say.

Q. What was the purpose of earning money with the use of the company equipment and not putting it through the company books?

A. That I can't say.

(Testimony of Vern Markee.)

Q. You were doing it, weren't you?

A. I was there, yes.

Q. You were in fact the controlling officer of the company, weren't you?      A. Yes.

Q. Well, why did you do it?

A. Well, we didn't have any adequate book-keeping system and I wasn't a bookkeeper myself, and it was——

Q. You knew it was going on?      A. Yes.

Q. Was it to defeat income tax purposes?

A. I don't know. [75]

Q. Was it to pay for your stock without building up a charge against you on the company books?

A. That I don't know.

Q. You were doing it. Why were you doing it?

A. I have often wondered myself. I don't know.

Q. Would you say as a practical matter that the difference between the credit that Mr. Heider shows on this mortgage and the amounts that you are charged with in the company books that that difference is the amount of company business that didn't go through the company books?

A. That I don't know.

Q. Did you secure any funds from any other source to pay Heider?      A. No.

The Referee: All payments to Mr. Heider were earnings from the company, is that right?

A. Yes.

Mr. Tonkon: I think there is one exception, your Honor. The \$5,000 that he paid went to Mr. Heider.

A. Both \$5,000 went to Heider.



(Testimony of Vern Markee.)

The Referee: One of them went to Mrs. Rand on the original purchase, is that right?

A. I believe that is right.

Q. (By Mr. Bollenbeck): Now, isn't it a fact, Mr. Markee, that the original mortgage was never set up on the books of the [76] company.

A. Yes, that is right.

Q. And that the second mortgage, the Public Utilities Commission insisted that the second mortgage be set up on the company books?

A. Yes.

Q. And at that time you, in order to set it up on the company books, you took this balance of \$13,168 that was still due on the first mortgage and you charged it to yourself on the company books?

A. I didn't do it, but it was done.

Q. That is what was done?

A. That is right, I recall that.

Q. And it was done with your consent and knowledge at the time it was done? A. Yes.

Q. Now, what is the value of that everywhere for hire permit that you are operating down there now? A. It has no value.

Q. Well, perhaps theoretically it doesn't, but actually what is it worth?

A. Well, it can't be mortgaged. It is just whatever anybody is willing to pay for it.

Q. You are giving the Rand Truck Line pretty severe competition down there aren't you?

A. I wouldn't say that. [77]

Q. What was your net earnings last year?

(Testimony of Vern Markee.)

A. \$8,000 about.

Q. That is off the truck line operation?

A. Yes.

Q. And before you went into competition with the Rand Truck Line was the Rand Truck Line handling that business that you are doing now?

A. Part of it.

Q. What big a percentage?

A. I'd say it's been 75 per cent of it.

Q. It could be 90 per cent, couldn't it, rather than 75? A. I don't think so.

Q. Did Mr. Heider draw up the original mortgage for you? A. I am not sure.

Q. Well, who did?

A. I say I am not sure.

Q. Who was your attorney at that time?

A. I don't believe I had an attorney unless it was Mr. Heider. He was handling—

Q. Now, as far as Mr. Heider paying the money to Rand, was that arranged prior to the time that this sale went through?

A. Well, that I don't know.

Q. You mean the Rands just agreed to give you their stock in this company in return for this note without knowing whether they could cash it in or not? [78]

A. Oh, we made an agreement with Mr. Rand to finance it. What arrangements he made—we made an agreement with Mr. Heider to finance it. What arrangements he made with the Rands I do not know.

(Testimony of Vern Markee.)

Q. But you talked to Mr. Heider and arranged for the financing of it, is that right?

A. That is right.

Q. And that was all, that arrangement was made before your deal with the Rands was finally completed?

A. Yes, it had been.

Q. So the Rands knew they were going to get their money from Mr. Heider before they sold the stock to you?

A. Yes.

Q. Now, let's go to the second mortgage. What was the occasion for having that executed?

A. To refinance.

Q. Why was that property of yours down there, that terminal building of yours, included in the mortgage?

A. Additional security.

Q. Had you owed Mr. Heider any money on that prior to that time?

A. No, sir.

Q. Had you owed him any money for any other reason prior to that time?

A. I had had dealings with him, yes.

Q. I mean unpaid, money that was unpaid at that time? [79]

A. No.

Q. When did you buy your house from Mr. Heider?

A. I believe it was in May in 1946 or '7, 1946.

Q. '46. That was prior to the time this mortgage was given. This second mortgage—in order that you won't be confused, it was executed the 7th day of August, 1946.

A. Well, I could be mistaken there.

Q. So you did buy the house from him a few

(Testimony of Vern Markee.)

months prior to the execution of this second mortgage?      A. That is right.

Q. And how much did you pay for this house?

A. \$9,400.

Q. You have a better memory than Mr. Heider. He couldn't remember this morning.

The Referee: He has been paying for it.

Mr. Heider: If the Court please, I don't want to be the least bit captious here, but this private transaction between us and Mr. Markee hasn't the slightest bearing on this, foreign entirely to it all.

The Referee: I don't either, but the examination permitted under the Bankruptcy Act is very broad.

Mr. Heider: I am amused by the house transaction because I can't see the slightest relevancy.

Q. (By Mr. Bollenbeck): How did you purchase this house from Mr. Heider, on a conditional sales contract or a mortgage? [80]

A. Mortgage.

Q. You took title to the property and give a mortgage back?

A. Yes, sir—I am not sure. Wait a minute. I would have to check.

Q. Well, what is the present balance on it?

A. Around \$5,000.

Mr. Heider: I still have the title.

The Referee: I figured Mr. Heider wouldn't take back a mortgage for the full purchase price.

Q. (By Mr. Bollenbeck): Now, let's talk about your terminal, Mr. Markee. When and where did you buy this land?

(Testimony of Vern Markee.)

A. I bought it from Mrs. Haas at Sheridan.

Q. That land was unimproved at that time, was it not? A. That is right.

Q. How much did you pay for it? A. \$900.

Q. And when did you pay for it, when did you buy it? A. About 1944, somewhere in there.

Q. Now, did you build a terminal on that land?

A. Yes.

Q. You built a building? A. Yes.

Q. And where did you get the money to build the building? A. I borrowed it from Mrs. Haas.

Q. As a matter of fact, you took it out of the company, didn't [81] you? A. No, I did not.

Q. Did you take any part of it out of the Rand Truck Line funds? A. I did not.

Q. Do you know that you are charged on the books of the corporation with a substantial number of hundreds of dollars for building the Sheridan terminal? A. Yes, I saw that.

Q. Well, what is your explanation of that charge?

A. That is not a just charge. It shouldn't be on there. Some of the stuff was purchased through Rand Truck Line but the money went back into Rand Truck Line.

Q. I don't understand your statement. You were in charge of the corporation at that time, were you not? A. At that time.

Q. And you had the opportunity and the right to dictate what should go into the books of the company, did you not? A. Yes.

(Testimony of Vern Markee.)

Q. And these charges were made against you?

A. It is \$1,300. I know what it is and it shouldn't be on there.

Q. Well, why didn't you have it corrected, then?

A. Too busy moving the freight, I guess.

Q. Now, do you know what it represents, the \$1,300? A. No, I do not. [82]

Q. If the company can produce vouchers to show that \$1,300 went into the Sheridan terminal would you still dispute the amount?

A. No. I told you it is \$1,300, and I know what it was.

Q. What was it then?

A. Material purchased for the terminal.

Q. What terminal?

A. For the terminal at Sheridan.

Q. Was that the terminal that was being built on your land? A. Yes.

Q. In other words, the company did purchase \$1,300 worth of stuff that went into that terminal?

A. The money went through the company books, the accounts went through the company books. The money was put back into the company.

Q. How was it put back into the company?

A. That was some of the money evidently that went to Otto Heider.

Q. You mean that you bought some materials to build your Sheridan terminal and they in order to repay the corporation for that \$1,300, you paid some money to Otto Heider, is that—

A. No, sir. The money went back into the com-

(Testimony of Vern Markee.)

pany and there could have been some of the money that went in to Otto Heider. I don't know.

Q. Could it have been some of the money that went to Otto Heider [83] in cash?

A. It could have been.

Q. That was the terminal where you afterwards leased to the Rand Truck Line, was it not?

A. That is right.

Q. And that was the terminal where you endeavored to secure a cancellation of about \$10,000 liability of yours in order to give them a lease, isn't that right?

A. They did sign a release on that, yes.

Q. What was the reason for demanding a \$10,000 bonus for signing a lease on your terminal?

A. I didn't consider that \$10,000 bonus. Mr. Taylor stated time and again that it was not a good entry on the book and should never have been on there, and when we—when we sold our stock to Rand Truck Line our lawyers suggested that we have Mr. Taylor give a release, which he did.

Q. You were on the books as owing Rand Truck Line over \$10,000, weren't you, for the money that went to Otto Heider?

A. That was—should have been the stockholders and not myself personally. Why they set it up in my name, I don't know.

Q. In other words, it should have been you and Loren Markee and Harold Macy?

A. The stockholders, yes.

Q. And the amount in fact is over \$27,000 when

(Testimony of Vern Markee.)

you add all three of them up, isn't it, the money on the corporation books [84] that went to Mr. Heider?

A. I am not sure it is that much. I believe that is what it was in the officers account.

Q. Well, you regard this cancellation of this \$10,000 item against yourself merely as a bookkeeping entry, is that what you understood it to be, just to clear the books? A. Mr. Taylor said——

Q. I am not asking what Mr. Taylor said. What did you think? Did you regard it merely as a bookkeeping entry?

A. No. The lawyer suggested that we get a signed release when we got out of Rand Truck Line.

Q. Who was your lawyer?

A. John Hickson.

Q. And you attempted to extract a \$10,000 bonus from the Rand Truck Line by the company cancelling your indebtedness to it in order to give them a lease in Sheridan?

A. I didn't consider it as such.

Q. They had been leasing that property prior to that time, hadn't they?

A. No, there hadn't been no lease on it up till then.

Q. They had been renting it from you?

A. That is right.

Q. What rent had they been paying?

A. \$50 a month.

Q. And what rent were you going to get under the lease? [85] A. \$50.

Q. You are using it yourself now? A. Yes.



(Testimony of Vern Markee.)

Q. And how long did that lease, how long did the Rand Truck Line occupy that terminal before you cancelled the lease?      A. Approximately a year.

Q. Why did you cancel it?

A. They broke their lease and didn't pay their rent.

Q. And did you sell your stock to Loren Markee?

A. Yes.

Q. And what did he pay you for it?

A. I got a '41 Chevrolet coupe.

Q. He gave you a '41 Chevrolet coupe for it?

A. I believe it was a '41.

Q. He gave you a '41 Chevrolet coupe for your stock in the Rand Truck Line?

A. That is right.

Q. Now, let's talk about the Delake terminal.

A. While we are on that stock, we might add that my wife didn't get anything for hers.

Q. She turned hers over to Mr. Taylor, didn't she?      A. After he insisted on it, yes.

Q. Now, the terminal at Delake is on leased ground, is it not?      A. Yes.

Q. In whose name is the lease, do you know? [86]

A. Mr. Thayer.

Q. I know, but it was signed by yourself personally or by Rand Truck Line?

A. I never saw the lease. The Portland manager at the time made the lease agreement.

Q. Now, who paid for building the terminal at Delake?      A. I paid for part of it.

(Testimony of Vern Markee.)

Q. How much of it did you pay for?

A. Approximately \$1,000.

Q. And who paid for the rest of it?

A. The rest of it was financed by the bank at Taft.

Q. Now, as a matter of fact the Rand Truck Line paid a lot of funds out to build that terminal, did they not?

A. Well, the only funds that they paid out were financed through the bank as far as I know.

Q. As a matter of fact, Mr. Markee, didn't Rand Truck Line pay out \$1,255.41 to help build that Delake terminal?

A. Well, the Delake terminal was built in two sections, the same way as the Sheridan terminal. The original section of the terminal I built myself and it cost approximately a thousand dollars.

Q. And how about the second section?

A. That was paid by the company.

Q. Paid by the company. In whose name—did you claim that you owned that terminal at that time? [87]

A. I owned a good share of it.

Q. And when you went to what is now the North Lincoln Bank and borrowed some money on it—

A. Mr. Taylor did that.

Q. Mr. Taylor did that. Didn't you borrow some money on that, the first mortgage on it?

A. Maybe I did.

Q. Borrowed \$1,500 on it, didn't you?

A. I believe that is right.

Q. And then you sold the terminal to the com-

(Testimony of Vern Markee.)

pany? A. No. Mr. Taylor took the terminal.

Q. Did you know that you had gotten a credit on your investment account for \$1,919 on the Delake terminal? A. That is right, yes.

Q. So you sold it to the company for \$1,919 subject to \$1,500 mortgage, or whatever the balance was on that \$1,500 mortgage, is that right?

A. Well, that was another one of these messed up deals. I had owned that terminal a year before this addition had been put on there for which I didn't receive any rent.

Q. Well, why didn't you receive any rent? You were controlling the company.

A. The company wasn't in a position to pay out any more money.

Q. That company paid for part of that terminal and then you sold it back to the company. [88]

A. I actually never got any money out of it.

Q. You got your indebtedness decreased, didn't you? It was entered as a credit to you.

A. Well, that officers account, yes, if you want to credit the officers account. I had \$1,000 of my own money in the terminal plus a year's rent coming at that time.

Q. Did you know that that credit was given to you on the books of the Company at the time it was made? A. Yes, Mr. Taylor told me.

Q. It was done with your knowledge and consent? A. Yes.

The Referee: You stated you had \$1,000 in the

(Testimony of Vern Markee.)

Delake terminal and a year's rent. What about the \$1,500? Did the Company borrow that or——

A. No. The Company borrowed that. The original terminal was built about 24 feet long and cost approximately \$1,000, and the mortgage, the money was borrowed on it after the terminal was enlarged and that is what that money was for.

The Referee: You didn't get any money on that \$1,500 mortgage?      A. No, sir.

(Chattel mortgage and note dated August 17, 1946, signed by Vern Markee, so produced, was thereupon marked Trustee's Exhibit 12.)

Q. (By Mr. Bollenbeck): Are you sure you are not mistaken about [89] not getting any money on this Delake terminal?

A. I didn't receive a dime.

Q. I am going to hand you Trustee's Exhibit 12, which is in amount \$1,300, dated August 17, 1946, in favor of you personally and also a note signed by you personally on the bank of \$1,300, on the Bank of Newport. Now, look that mortgage over and see if you can't refresh your memory as to whether you personally didn't get some money on that mortgage.

A. No, sir. If you check up on the books you will find it cost around \$1,300 to \$1,500. That was paid to Beverage & Hart. I don't know whether it is on the books or not, but that is what the bill was because the money was borrowed after the bill was submitted.

Q. Now, who are Beverage & Hart?

(Testimony of Vern Markee.)

A. That is this construction contractor, building contractor.

The Referee: Was that for the second addition?

A. Yes. The first addition was paid for at the time it was built by myself.

Q. (By Mr. Bollenbeck): And this was supposed to pay for the second part, is that right, in addition to what money the company paid out, this \$1,300 plus the \$1,255 that the company paid, is that supposed to pay for the second addition?

A. I didn't know the company paid out twelve hundred and some dollars.

Q. We have got the officers account charged, you charged with [90] \$1,255 for building the coast terminal.

A. Well, I don't know how that could be set up there because the money, after we received a statement from Beverage & Hart I went down to the bank and the banker loaned enough money to pay the construction cost. Where that \$1,200 in the coast terminal—Beverage & Hart also built the McMinnville terminal, but what the \$1,200 is doing on there I don't know. I am sure I didn't get any of it.

The Referee: Mr. Bollenbeck, have you quite a number of questions? We will have a recess if you have.

Mr. Bollenbeck: I would like a recess.

(Short recess.)

Q. (By Mr. Bollenbeck): I want to hand you Trustee's Exhibit 11, Mr. Markee, which is the bill

(Testimony of Vern Markee.)

of sale that you gave Rand Truck Line and particularly refer you to one Chevrolet panel 1941 half-ton truck, and ask you if you know what happened to that truck.       A. That was sold.

Q. What was the amount that you received for it?       A. Approximately \$600, I believe.

Q. Are you sure it wasn't \$800?

A. I am not sure whether it was \$600 or \$800.

Q. What happened to the money?

A. That was used in the business.

Q. Are you sure it wasn't used to purchase a 1938 Ford for [91] yourself, purchased, by the way, from Mr. Otto Heider?

A. I believe that is right.

Q. That is right. And did you take title to that '38 Ford in your own name?       A. Yes.

Q. Although the Chevrolet was a company asset?

A. Yes. It is one of the pieces of equipment that I turned in when I went into it.

Q. And what happened to the '38 Ford?

A. That was traded on a car.

Q. You traded it in on a Cadillac, didn't you?

A. Yes, that is right.

Q. Have you still got the Cadillac?       A. No.

Q. What happened to the Cadillac?

A. That was sold.

Q. What happened to the money from that?

A. It went into the Sheridan terminal.

Q. Well, now, when did all this happen? I thought the Sheridan terminal was paid for by the thousand dollars you put into it and the \$1,300 that

(Testimony of Vern Markee.)

you say you paid to Beverage & Hart and the \$1,300 or so charged against you on the company books. Now, did it cost that much more to build that terminal?

A. That Beverage & Hart deal you are referring to is on the coast terminal. [92]

Q. Oh, pardon me. This terminal at Sheridan cost \$8,000. So in addition to the money shown on the books charged against you and shown as going into the Sheridan terminal we have an additional six or eight hundred dollars of company funds that went into the Sheridan terminal, is that right?

A. Well, there is approximately a year there wasn't any rent paid on the Sheridan terminal too.

Q. I am not asking about that. This went into the building of the terminal? A. Yes.

Q. Now, when you left Rand Truck Line you took another Chevrolet along with you, didn't you?

A. Yes.

Q. And where did that car come from?

A. That was my own original property.

Q. How long had you had it?

A. About a year and a half.

Q. From whom did you buy it?

A. Either Smith or Fields in Portland.

Q. And how did you pay for it?

A. Paid for it with cash.

Q. How much cash? A. Around \$1,800.

Q. Where did you get the cash?

A. Do I have to answer all these questions? [93]

The Referee: Yes, you have to answer even that.

(Testimony of Vern Markee.)

A. I sold my house here in Portland.

Q. (By Mr. Bollenbeck): How much did you sell your house in Portland for? A. \$11,000.

Q. Did you put the money in a bank account?

A. After the mortgage was paid, yes, I put the balance that I had left in the bank account.

Q. How much was your mortgage?

A. I am not sure. I believe I realized about \$2,500 out of it.

Q. You realized after payment of the mortgage about \$2,500? A. Yes.

Q. What bank did you put the money in?

A. It was either the First National of Portland or at Sheridan.

Q. And out of that \$2,500 you paid how much for this Chevrolet?

A. Seventeen or eighteen hundred dollars.

Q. Where did you get the \$8,000 to build the Sheridan terminal?

A. Borrowed it from Mrs. Haas.

Q. Well, how much did you borrow from her?

A. Oh, I borrowed \$2,500 the first time and then two years later I borrowed about \$5,000.

Q. I am talking about the money to build it. Now, you didn't wait two years to build it.

A. Well, both terminals were built on the same deal. They were built 24 by 30 to start with and they were both enlarged. [94] This one, the building at Sheridan is now 26 by 118.

Q. In other words, you say that you borrowed



(Testimony of Vern Markee.)

\$2,500 from this Mrs. Haas—how do you spell her name?      A. (Spelling) H-a-a-s.

Q. Where does she live?

A. She lives at Sheridan.

Q. What is her first name or initials?

A. L. Letitia. She is the one that owned the property.

Q. Letitia Haas?      A. Yes.

Q. You borrowed \$2,500 from her first?

A. Yes.

Q. And when you enlarged the terminal you borrowed \$5,000 more from her?

A. I don't believe it is quite \$5,000.

Q. Did that \$5,000 include the original \$2,500?

A. No.

Q. How much of a mortgage is against it now besides Mr. Heider's mortgage?

A. I believe Mr. Heider's mortgage has been released.

Q. You mean this Rand Truck Line mortgage against your property has been released?

A. I believe that is right, Mr. Heider.

Mr. Heider: I think maybe it is part of the lease file on the real estate. [95]

Q. (By Mr. Bollenbeck): When was that filed, do you know, Mr. Markee?

A. I don't know whether it was filed or not. I know it was included in the mortgage and after the mortgage was paid off a little bit I believe Mr. Heider released it.

(Testimony of Vern Markee.)

Q. Did you pay him anything for the release of it? A. No, sir.

Q. How much of a mortgage has Mrs. Haas got against it? A. She has around \$4,000 now.

Q. Now, how much did you pay to Mr. Heider as a down payment upon your home? A. \$1,500.

Q. And you bought that at the time you were still with the Rand Truck Line? A. That is right.

Q. Where did you get that money?

A. The balance of what money I had left over selling the other place and I had some.

Q. That was approximately \$700. Where did you get the rest of it?

A. I had some money in the bank.

Q. What bank? A. Bank of Sheridan.

Q. About \$1,000?

A. I paid Mr. Heider \$1,500. [96]

Q. Well, you had \$500 left over from your house sale here in Portland, is that right? You had about \$1,000 in the bank? A. No, sir.

Q. Where did you have the money, where did you get the thousand dollars?

A. Well, I said I had some of it in the bank.

Q. Well, how much of it did you have in the bank?

A. Oh, I don't remember now. All I can remember is I paid him \$1,500.

Q. Well, I want to know where you got it.

A. Well, I earned it. That was three or four years ago. I sure didn't take it from Rand Truck Line, if that is what you are driving at.

(Testimony of Vern Markee.)

Q. Now, Mr. Markee, did you establish an account down at the North Lincoln Bank at Taft, Oregon? A. Yes.

Q. And that was in substance an account in Rand Truck Line's name and your name too?

A. Yes.

Q. And you could draw personal checks on that account? A. Yes.

Q. And Rand Truck Line could draw business checks on that account?

A. Just through the other office.

Q. Well, they could use that account to transmit funds to [97] Portland? A. That is right.

Q. And you could use it for your personal account, is that right? A. That is right.

Q. And Rand Truck Line money went into that account, didn't it? A. Yes.

Q. And did you put any money into it yourself?

A. Yes.

Q. Do you have the statements on those accounts?

A. No.

Q. Do you know where they are? A. No.

Q. Are you sure you didn't get this \$1,000 to pay or \$1,500 to pay Mr. Heider out of that account?

A. Yes, I am very sure.

Q. Well, what account did you get it out of?

A. I had some money of my own.

Q. Where? A. In the bank.

Q. What bank? A. The bank at Sheridan.

Q. Do you have your cancelled checks and bank statements? A. I have some of them, yes.

(Testimony of Vern Markee.)

Q. Can you produce them, produce this \$1,500 check that you paid [98] to Mr. Heider?

A. Yes, sir.

Mr. Bollenbeck: I would like to ask an order of the Court to produce that at the same time he produces that agreement.

A. That agreement is coming right up.

The Referee: Mr. Hickson is bringing that over.

Q. (By Mr. Bollenbeck): Now, what was the reason of mixing company funds and your personal funds down there in that North Lincoln Bank?

A. Well, it didn't make any difference. All the accounts that were down on the coast at the time I was down there I was responsible for and they were all paid.

Q. You mean the accounts payable?

A. The accounts payable.

Q. What about the accounts receivable?

A. Well, all the accounts receivable went into the checking account and all the freight bills were charged out against that division.

Q. As a matter of fact, Mr. Markee, when you left that division down there there were a lot of apparently uncollectible accounts receivable that had in fact been collected?

A. Definitely there were quite a number of them.

Q. And who was responsible for that condition?

A. The fellow that was down there before I went down there.

Q. Mr. Robinson?

A. That is right.

(Testimony of Vern Markee.)

Q. And were any of those during your time down there?

A. Every bill that was down there while I was down there was paid when I went out there.

Q. I am talking about your accounts receivable. Now, there were a lot of accounts receivable down there that the money never went into the company books.

A. That is right.

Q. And where did the money go that didn't go to the company?

A. Mr. Robinson had been down there and collected around \$4,000, if I remember.

Q. Did Mr. Robinson work for you down there, Rand Truck Line?

A. No, sir, he did not.

Q. Did he continue to work for you when you went down there?

A. He did not.

Q. Was there any money of Rand Truck Line during your stay down there that was diverted?

A. Definitely not.

Q. Was Robinson under bond at the time he was down there?

A. No.

Q. Didn't you have your employees under bond?

A. No, sir. To clear the record there, I was only down to the Coast myself for around twenty-five days.

The Referee: You have a right to explain any answers that [100] you want.

A. The reason I went down there is that this man went down and skipped out and left a mess and I went down and straightened it out, and before I left I put a responsible man in the position and set-

(Testimony of Vern Markee.)

tled up all the accounts that were charged out while I was down there taking care of that territory.

Q. (By Mr. Bollenbeck): Where did the bank statements and the cancelled checks from that joint account, yours and the Rand Truck Line, where did they go to?

A. I don't know. The Agent probably picked up some of them. I never got them.

Q. You mean you never got your personal cancelled checks back?

A. No. When I left there, why, when they had that fire at McMinnville, and I went back down to McMinnville and didn't get back out to the Coast until some time later.

Q. Did you take all of your personal money out of that account?

A. I didn't have any personal money in there at that time.

Q. Personal money of yours had gone through that account? A. That is right.

Q. But at the time you left you didn't have any personal money in?

A. That is right. All I deposited in there was my pay checks.

Q. Who reconciled that account, who balanced it?

A. Mr. Taylor.

Q. How could it be balanced with your personal funds in there? [101]

A. That was simple. Everything that was down there was charged up to me and I paid for it.

(Testimony of Vern Markee.)

Q. When was this account in existence down there?

A. Just before the fire when the terminal burnt at McMinnvile.

Q. Neither the Judge nor I know when that fire occurred. Can you tell us by calendar months and dates?

A. I believe it was in June, about 1946. I am not sure. Mr. Taylor can tell you.

Q. Was he with the company at that time?

A. No.

Q. So he wasn't with the company at the time this bank account was established and in existence?

A. No.

Q. And who did balance that bank account?

A. Mr. Taylor.

Q. Well, how long was it in existence?

A. Around twenty days or so.

Q. You mean you went down there and established a bank account for yourself and the company and put company money in it and put your money in it and closed the account out all in twenty days?

A. No, I didn't say it was closed out. It was used for about twenty days, and it wasn't closed out until some time later. When the terminal burned in McMinnvile we forgot about everything else and when the agent took off, then, when the men took [102] over when I left, why, we started a different bank account. He wrote checks payable only to Rand Truck Line, McMinnvile.

The Referee: Mr. Bollenbeck, Mr. Hickson is

(Testimony of Vern Markee.)

here now and he has that agreement if you want to look at it.

Mr. Bollenbeck: Yes, I would, yes.

Q. By this agreement, Mr. Markee, you were selling out the Markee Truck Line for \$9,000 and the Rand Truck Line agreed to pay your debts in the amount of about \$3,000 and issue you 25 shares of stock of par of \$100. I think that was what was really done, they really did issue you 500 shares of stock with a par of \$10. A. \$5,000.

Q. So they issued you \$5,000 worth of stock and \$3,000 they assumed your liability.

A. There is no consideration in there for any permits, which you was trying to get out of me awhile ago.

Q. Well, that was a part of the whole agreement, wasn't it, a transfer of the permits to them?

A. No, sir. There was no consideration in there in that \$9,000 for any permits.

Q. You have been talking to your lawyer about "no consideration," but it was a part of the whole deal that you were to assign the permits to them. It provides in here as a part of this sale "Sellers do hereby promise to sell and assign to the purchaser all PUC permits and Interstate Commerce permits for [103] the operation of trucks as common carriers." That was part of your agreement to assign and set over, and you further provide that if you cease to become a stockholder then at his request Rand Truck Line agrees to assign and set over said



(Testimony of Vern Markee.)

permits now owned by Rand Truck Line to the said Vern Markee.

A. That is right. That is the only way we would consider going into partnership with Bob Rand.

Q. Well, now, this agreement in addition provides, Mr. Markee, that as long as you are a stockholder of the Rand Truck Line that you do not engage in any business in competition with the Rand Truck Lines.

Mr. Hickson: Your Honor, I wonder if I could have an appearance in behalf of Mr. Markee. My name has been dragged in by counsel here.

The Referee: There is no need for an appearance. No issue before the Court. We are merely getting at the facts, Mr. Hickson. Mr. Markee has been brought in under subpoena under Section 21-a of the Bankruptcy Act and to be examined in regard to his transactions with the Rand Truck Line. There is no issue, nothing involved at this time except to get at the facts.

Mr. Hickson: May I suggest possibly the contract is the best evidence and should be shown to the witness.

The Referee: Well, I think that should be done.

Mr. Bollenbeck: Well, if there is any question as to whether [104] I was reading it correctly, I will be glad to.

The Referee: There is no issue at this time. We have asked him to produce the contract and we would like to have a copy of it in evidence. Introduce this but substitute a copy.

(Testimony of Vern Markee.)

Mr. Hickson: Your Honor, I will need that in another proceeding before the PUC, so I would like to have that, substitute a copy.

Mr. Tonkon: Just a minute. I suggest you have that marked and introduce it.

(Copy of contract between Mr. Markee and Mr. Rand, so produced, was thereupon marked Trustee's Exhibit 13.)

Q. (By Mr. Bollenbeck): Mr. Markee, when did you start operating down at Sheridan after you ceased taking an active part in the Rand Truck Line?

A. The permit was reinstated in August of 1947.

Q. When did you cease to be a stockholder of the Rand Truck Line?

A. The last of February, 1948.

Q. For a period of several months you were operating in competition with the Rand Truck Line and were still a stockholder of it, is that right?

A. Yes. I might add that anything we hauled could have been hauled by thirty or forty other carriers located here in the [105] City of Portland during that time. As far as that goes, it could have been hauled by any one of a hundred carriers within this vicinity.

Q. Now, Mr. Markee, do you know of a shipment that went to a Mr. Forrester down at Daleyville, Oklahoma?

A. Yes.

Q. Did you collect the money for that shipment?

A. Yes.

(Testimony of Vern Markee.)

Mr. Hickson: Mr. Referee, may I ask a question? I am wholly unfamiliar with your procedure, but it is perfectly obvious to me in the short time I have been here that Mr. Taylor here and counsel are trying to lay the grounds for a damage suit that is pending out at McMinnville against Mr. Markee. It hasn't anything to do with this case.

The Referee: Any transaction of this man with the corporation is relevant here. That is all I want, and he is not entitled even to counsel.

Mr. Hickson: That is all I wanted to know.

The Referee: All we do is get at the facts.

Mr. Hickson: I just wanted that in the record.

The Referee: If there is any issue brought up later, why, the matter can be gone into at that time.

Q. (By Mr. Bollenbeck): Now, that shipment to Oklahoma was handled through the Rand Truck Line, was it not? A. Yes. [106]

Q. And you collected the money for the entire shipment? A. Yes.

Q. Still have retained it? A. That is right.

Q. I understand you refuse to pay it over to the Rand Truck Line?

A. I didn't refuse to pay it. I will pay it if they will render a statement just like any other business house instead of hitting me up on the street for it.

Q. Who hit you up?

A. Who do you suppose? Mr. Taylor.

Q. As a matter of fact Clayton Markee asked you for it?

A. Clayton Markee has asked me for it.

(Testimony of Vern Markee.)

Q. If we submit you a statement will you pay the same?

A. The money is in the bank waiting for a statement. If you get it in before the 10th it will be paid on the 10th.

The Referee: Anything else now?

A. I would like to add here too that there is plenty of business in this territory between here and the Coast for two or three truck lines, but it seemed that Rand Truck Line owned it all and nobody else had any rights down there to haul anything, and instead of them getting all, why, they come out on the short end of it, and they are trying to blame me for it. We have never solicited any business any time we have been in business down there. We haven't had to. We have had more than [107] we can take care of. And I don't want to take the blame for somebody's bull-headedness.

The Referee: Have you any other questions?

Mr. Bollenbeck: I think that is all.

The Referee: All right, Mr. Markee. Thank you very much.

Mr. Bollenbeck: The Court indicated earlier in the day that they were going to adjourn this meeting.

The Referee: Well, now, what else do you want?

Mr. Bollenbeck: There were some bank statements, your Honor.

The Referee: No, there was only a cancelled check that he was going to show that he paid to Mr.

(Testimony of Vern Markee.)

Heider for the purchase of his property. That was the only other thing, wasn't it?

Mr. Heider: If the Court please, I will verify what Mr. Markee said about that. That was right. He paid me \$1,500 down on the place. I know that is what the check would show if it was produced here. Since he mentioned it I am certain that is what it was. And the figures he give on the place, as you say, he was doing the paying there and they are more accurate than my figures. I am sure they are.

Mr. Bollenbeck: I have no special desire to have it continued, your Honor.

The Referee: All right, I will not continue it at this time. I think if we should want any further information Mr. Markee will probably come voluntarily, won't you, Mr. Markee? [108]

A. Yes, sir.

The Referee: Thank you. Then, this matter will be adjourned and you will proceed to prepare the order for the sale of the assets free from liens.

(Witness excused.)

Mr. Bollenbeck: There is one question, your Honor. It just occurred to me that I would like to ask Mr. Markee—I don't know—Mr. Markee, are you attempting to negotiate the purchase of the mortgage on the Delake terminal?

Mr. Markee: No.

The Referee: That is all.

(Hearing adjourned.) [109]

## Certificate

I, Glenn G. Foster, hereby certify that on Wednesday, July 6, 1949, I reported in shorthand certain testimony and proceedings had in the above-entitled cause; that I subsequently caused my said shorthand notes to be reduced to typewriting, and that the foregoing transcript, consisting of 109 pages, numbered 1 to 109, both inclusive, constitutes a full, true and accurate transcript of said testimony and proceedings, so taken by me in shorthand on said date as aforesaid, and of the whole thereof.

Dated this 28th day of July, A.D. 1949.

/s/ GLENN G. FOSTER,  
Court Reporter.

[Endorsed]: Filed July 28, 1949, Referee.

[Endorsed]: Filed October 23, 1956, U.S.D.C.

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March 14, 1956, 10:00 A.M.

The Referee: This matter comes on upon the objections to the claim of Otto Heider. I believe it was originally set for hearing February 28, 1956, at 2:00 p.m., and by the consent of counsel it was continued to be heard at this time and date.

Mr. Dougherty: May the record show on behalf of the Creditor Otto W. Heider, we would like to submit at this time a motion to dismiss, on the ground that the controversy involved here has, by authority of the Referee, been submitted to the Circuit Court of the State of Oregon for Multnomah

County, and is now pending. It is our understanding that the complete controversy was submitted to that court, and thereby this Court deprived itself of jurisdiction in the matter.

We move for dismissal of the objections on this added ground: A prior hearing in this matter was held, I believe in June of 1949——

Mr. Miller: July 6, 1949.

Mr. Dougherty: We are now nearly seven years after that time. At that time the Referee stated that if the Trustee had [2\*] any objections to the claim that the Trustee would file such objections. They were not, as a matter of fact, filed for nearly seven years after that. Accordingly, I believe there's been undue laches, which has had a very material adverse effect upon the creditor, and that the stale objections should not now be heard.

Mr. Miller: If the Court please, we haven't read this motion to dismiss ourselves, your Honor, but I think it goes without saying that this Court can never rob itself of jurisdiction under 57 of the Bankruptcy Act, to hear a claim.

There is a possibility that there are questions in the Circuit Court matter, some of which this Court would never have had jurisdiction over. Notwithstanding that, however, and even if it were possible for the Court to rob itself of jurisdiction here, which I don't believe is possible under the Bankruptcy Act, the proceeding over there has never come to trial; there is no adjudication over there, and hence

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\*Page numbering appearing at top of page of original Reporter's Transcript of Record.

the matter certainly isn't *res judicata*, or anything like that, and I think that the Court, at any time prior to a judgment over there, would retain jurisdiction to hear those matters which are designated to this Court by the Bankruptcy Act, and that is all that is here.

Now, with regard to the time elapsed, there is nothing in the Bankruptcy Act which says when a bankrupt may file objections. He may file objections at any time before closing of a case, and without taking a lot of time I will say if there has [3] been delay here, the record in the Circuit Court will show the delay has been as much on the part of the Claimant as of the Trustee. The great length of time between the pleadings due over there and the time within which they were filed will take many years. I don't think he is in good faith here when he talks about laches.

Mr. Dougherty: If the Referee please, I would like to take exception to counsel's comment. In the first place, the counsel who made the comments doesn't have knowledge in the matter, and in the second place, it is true that counsel for the Trustee was required to file, I believe, five different complaints, many of which were found to be insufficient upon demurrer, by the Court, and the last thing that happened was in October of last year, when the Trustee's demurrer to our affirmative answer in that proceeding was overruled. Since that time my file indicates that the Trustee has not taken action.

This identical question was presented to the Circuit Court on that demurrer, the question being



whether or not the entire controversy had been submitted to that court, and the judge, by his ruling and by his comments from the bench, indicated that he considered that it had. It may be as a technical matter that this Court retains jurisdiction. I don't believe that it does, but even assuming that it does, I think as a matter of comity between courts this Court should not exercise any jurisdiction while the matter is still pending before the [4] Circuit Court, and I believe there is no question that identical issues are involved even though the proceeding in the Circuit Court involves other parties and additional issues.

Mr. Bollenbeck: Now, if the Court please, I would like to answer counsel. The demurrer was sustained—or overruled, rather, by Judge Dobson in the Circuit Court. One of the things that was not before the Court at that time was that Otto Heider had filed a claim here. That was not in the complaint, it was not in the answer—I mean it was not in the demurrer. I demurred to the affirmative counterclaim and there was no allegation in the counterclaim that this claim had been filed by Otto Heider. It was, therefore, not in the record that he had submitted to this Court's jurisdiction first. The case is now pending over there on a plea in abatement to the counterclaim, in which plea in abatement I did set up that this claim had been filed in this Court.

In other words, if there is a conflict in jurisdiction it is a conflict that is created by Mr. Heider's own act. He submitted to this jurisdiction, to this Court, and then attempted to raise the same issue over

there, and as I said, the demurrer did not and could not show that this claim had been filed. The plea in abatement does show that this claim had been filed.

Now, the issues are these: The pleadings are different and the dates are different. It is an entirely different question [5] over there, and at that time I briefed the law, and the law, I think, is plain that this Court, even with the Referee's consent and everybody's consent, cannot release its jurisdiction. This is the only court that can determine how the assets in its possession are to be disbursed. The state courts have concurrent jurisdiction in the collection of assets, which is what that case is about. This is the reverse of the picture, a picture on the distribution of the assets, that the Court has in its possession now.

The Referee: Let me clear up one question in the record. Mr. Dougherty spoke of a hearing on this matter in July of 1946. That was——

Mr. Miller: 1949, your Honor.

The Referee: 1949? What was the nature of that hearing? Was that an examination——

Mr. Bollenbeck: That was an examination of Mr. Heider and Mr. Vern Markee, and it involved much more than is here.

The Referee: Under Section 21-a of the Bankruptcy Act.

Mr. Dougherty: If the Court please, reading from the transcript, your Honor at that time said, "We expect to sell it" (meaning the property on which Mr. Heider had liens, and he has turned over those evidences of title)—"We expect to sell it for

considerably more than the amount you claim, and the matter of determining the validity and amount of your lien will be taken up and if the Trustees have any objections to it you will [6] be served with the objections and then there will be a further hearing on it." Those objections weren't filed for over 6 years later.

The Referee: Well, I think that is due to the fact that in the state court where the issues are enlarged, they were weighing whether they could determine in the state court, but this court is not accustomed to waiting 6, 7, and 10 years to get things determined. The purpose of the Bankruptcy Act is to liquidate the assets as quickly as possible and see that they are paid to the creditors according to the equities of the case and pro rata to the general creditors. I think Mr. Heider is just as anxious as the rest of us to try to get this matter determined once and for all. The only matter before this Court is the validity of his claim and the mortgage securing his alleged claim. I don't think this Court can relinquish paramount jurisdiction to determine that matter.

I suggest that we proceed and see if it can be determined at this time. Mr. Heider has the right of review. It can be quickly granted to him if he should not be satisfied with the Referee's determination, so you may proceed.

Mr. Bollenbeck: Do I understand it is the Trustee's duty to go forward first?

The Referee: That's right.

Mr. Miller: If the Court please, in the interest of

conservation of time, if the examination of July 6, 1949, of Mr. Heider [7] is not deemed part of the record in this case, we would ask that it be deemed part of the record of this hearing.

The Referee: You mean the examination?

Mr. Miller: The examination of Mr. Heider. It would save a lot of time going over the same matters that were gone into on that date.

Mr. Dougherty: It is my understanding, your Honor, that it was a part of the record.

The Referee: You stipulate that it may be made a part of the record in this hearing?

Mr. Dougherty: Yes.

Mr. Bollenbeck: Call Mr. Rand, please.

The Referee: Mr. Rand, will you come around here, please? Your full name, please.

Robert R. Rand: My full name is Robert Roy Rand.

#### ROBERT R. RAND

was thereupon produced as a witness in behalf of the Trustee and, being first duly sworn, was examined and testified as follows:

#### Direct Examination

By Mr. Bollenbeck:

Q. Mr. Rand, at one time you and your wife were majority stockholders in the Rand Truck Line, were you not?      A. Yes, sir.

Q. And what percentage of the stock did you own, do you remember?

A. Repeat the question.

(Testimony of Robert R. Rand.)

Q. What percentage of the stock did you own, do you remember? A. Eighty per cent.

Q. And who owned the rest of it at that time?

A. At the time we sold out?

Q. Yes. A. Mae Potts.

Q. Who was Mae Potts?

A. A sister-in-law.

Q. Now, did Vern Markee become a minority stockholder in your corporation shortly before you sold out? A. Yes, he did.

Q. And did you and he conduct negotiations for the purchase of your stock and Mrs. Potts' stock?

A. Yes, he did.

Q. And did you arrive at a deal?

A. Yes, we did.

Q. And what was that deal?

A. He was to pay me for the 80 per cent, after Vern became a third partner, or a third stockholder in the corporation—and he agreed to purchase all of the stock that we owned, both myself and Mrs. Potts.

Q. And how much money was he going to pay for it?

A. He was going to pay \$40,000 for it. [9]

Q. And did he have \$40,000?

A. I wouldn't know.

Q. Well, did you discuss the financing arrangements with him as to how this forty thousand was to be paid? A. Yes.

Q. And what decision did you arrive at, or what action did you take?

(Testimony of Robert R. Rand.)

A. He was going to finance it and pay me in a way that would be satisfactory to me.

Q. And how was he going to finance it, or how did he finance it?

A. Well, he borrowed the money and paid me.

Q. From whom did he borrow the money?

A. He borrowed the money from Otto Heider.

Q. When did Otto Heider first appear in the picture in this transaction?

A. At the time of the negotiations. I don't remember the exact day or anything, but he was a party to the negotiations. He had to O.K. the payment of the money.

Q. Was it before the deal was closed?

A. Well, no. Vern and I closed the deal.

Q. Well, was it before the papers were signed on the deal?

A. Of course it would have to be. The finances were arranged before the deal was closed.

Q. And did Mr. Heider know what the deal was?

A. I am quite sure he was familiar with it. [10]

Q. And Vern was buying your stock?

A. I am quite sure he was familiar with it. I can't say for sure.

Q. And did you and Vern discuss it in his presence?

A. I don't think ever; I don't think ever the three of us met at any one time.

Q. Do you know where the papers were prepared, the mortgages and so forth?

(Testimony of Robert R. Rand.)

A. Well, there never was any papers prepared, actually excepting a contract.

Q. Who prepared the contract, do you know?

A. Otto Heider's office.

Q. Otto Heider's office. When was that? What was the contract for?

A. For the payment of the money.

Q. Between you and Otto Heider?

A. No, between Vern and I. Otto Heider had nothing to do whatever with the negotiations. He was purely and simply—it was through his organization that the thing was financed, but personally Otto Heider had nothing to do with it.

Q. Yes, but did he represent either you or Mr. Markee in this transaction?

A. You mean as a legal attorney?

Q. Yes.

A. No, it wasn't necessary. We needed no advice or attorney to handle the negotiations. [11]

Q. Now how were you paid, Mr. Rand? I mean how much, if any, cash did you receive?

A. I received \$8,000 in cash and the balance on a contract.

Q. You received \$8,000 in cash at the time the deal was closed?

A. I don't remember any more just when I received it but I am sure that I would have received it at that time.

Q. And the balance was paid in payments of \$500, wasn't it?

A. Five hundred dollars a week, yes, sir.

(Testimony of Robert R. Rand.)

Q. Five hundred dollars a week—\$32,000 was paid in that fashion? A. Plus interest.

Q. And Mr. Heider paid you some interest on that payment that was made?

A. Yes, he did.

Q. I want you to look over these checks, Mr. Rand, and I'll ask you whether those are the checks—I don't think you got all of them, but will you look over those checks and see whether those are the checks that Mr. Heider issued to you?

A. (Examining checks): This check doesn't have my signature.

Mr. Bollenback: He is referring now to a check dated November 2, 1945, in the amount of \$5,000, signed by Otto Heider, payable to Vern Markee and the Rand Truck Line.

A. Here is also another one, but I think there must be a slip-up on this, but it doesn't have my signature on it.

Mr. Bollenback: He refers now to a check dated——

Q. Well, the check is payable to you, Mr. Rand, and to your wife. [12]

A. Well, the bank shouldn't have cashed it in that way. It was endorsed by neither one of us.

Mr. Bollenback: For the record, this check is dated December 2, 1944, payable to R. R. Rand and/or Goldie I. Rand, \$500. It has a penciled notation on the front, "Ind. missing," and on the back it says: "Placed to the credit of within named



(Testimony of Robert R. Rand.)

payee. Endorsement guaranteed. The First National Bank."

A. Well, that apparently clears it up. Those two checks I don't recognize. The others I think were the original checks that I endorsed and received in payment.

Q. Will you count them, Mr. Rand? They are all \$500, aren't they, except the interest checks?

A. I didn't check that.

Q. Eliminating the interest checks, count and see how many there are.

A. (Counting): Sixty-three, I count.

Q. That would be \$31,500?

A. Unless I overlooked one.

Q. Actually that is my count too, Mr. Rand.

A. Well, I believe that——

Mr. Dougherty: Will counsel extend me the courtesy——

Mr. Bollenback: Yes, I was just going to put a rubber band around them.

Mr. Miller: If the Court please, while Mr. Dougherty is looking at that, I just handed him a supplemental objection. I apologize [13] for the lateness, but it doesn't change any of the facts.

Mr. Dougherty: We will object to its being received at this time.

The Court: We will go into that later.

Q. (By Mr. Bollenback): Mr. Rand, what did the corporation receive in return for the execution of this note and mortgage?

Mr. Dougherty: If he knows of his own personal

(Testimony of Robert R. Rand.)

knowledge. A. The question again, please?

Q. What did the corporation receive in return for the execution to you and your wife of this note and mortgage in the amount of \$43,560?

A. I don't know. I don't understand it. I don't understand what note you refer to.

Q. Well, I will hand you Trustee's Exhibit 3, which is a promissory note signed by the Rand Truck Line, Inc., payable to Mrs. R. R. Rand, in the amount of \$43,560, and ask you what you gave the corporation in return for that note and the mortgage that secured it?

A. I didn't sign this note and I can not—it is unfamiliar to me. I never saw the note before, as far as I know.

Q. You never saw the note before?

A. I never saw the note before as far as I know. As far as I can remember I have never seen the note before.

Q. Did you and your wife discuss this transaction? A. Yes, we did. [14]

Q. Can you tell me why she endorsed this note "Without recourse or liability?"

A. Well, the only reason that she would have the authority to do it was that she was secretary of the Rand Truck Line and she would have authority to do it.

Q. Mr. Rand, maybe you misunderstand the situation. This is a note and mortgage that was given to you and your wife personally, not to the corporation.

(Testimony of Robert R. Rand.)

Mr. Dougherty: I object to the form of the question. The note shows on its face that it wasn't given to this witness.

The Referee: Has that note been received in evidence?

Mr. Bollenback: It was received at the other hearing, your Honor.

Q. Well, Mr. Rand, let me ask you this: Was there any discussion between you and the other parties as to whether this should be payable to you or to your wife?      A. No.

Q. There wasn't?      A. No.

Q. I am going to hand you Trustee's Exhibit 6, together with a carbon copy of it, and ask you whether or not the title "Mrs" wasn't inserted after the mortgage was typed up. I refer to this line, right here (pointing), about the seventh line down.

A. The only excuse I could offer for that, I went on a hunting trip and I told Mrs. Rand at the time that I left, if it was [15] necessary to sign any papers that she could go ahead and sign them, and this might have happened at the time I was on the hunting trip.

Q. Then it was contemplated that this originally was to be payable to you, is that right?

A. To either one of us.

Q. To either one of you?

A. To any one of the stockholders of the corporation. It was actually paid to each stockholder and divided.

(Testimony of Robert R. Rand.)

Q. Now, can you tell me why this endorsement is on here, "Without Recourse or Liability?"

A. I don't know. This is Mrs. Rand's signature.

Q. It is her signature?

A. It is her signature.

Q. And to your knowledge you never saw that note before?

A. I don't recognize this note. I am sure I have never seen this note before.

Q. Well, now I am going to ask you again, what did the corporation get in return for executing a mortgage payable to your wife—you say you are fully familiar with the situation—payable to your wife?

A. No, I didn't make a statement I was fully familiar.

Q. Well, you said the transaction contemplated that the mortgage was to be delivered to you.

A. No, I said there was never any mortgage. The thing was sold [16] on a contract. This document, I don't think was ever in my possession. As far as I know it was never in my possession. I held the stock of the corporation until each one of these checks was cashed and that was all the security that I needed. I held in my possession the stock of the entire corporation until such time as the last one of these checks was cashed and it cleared the bank.

The Referee: You are referring to Mr. Heider's checks?      A. Yes.

Q. Now, Mr. Rand, referring to Trustee's

(Testimony of Robert R. Rand.)

Exhibit 7, which is the minutes of the corporation, and I refer you to a stockholders' and directors' meeting held September 28, 1944, in which it is recited that you, your wife, Vern Markee, Florence Markee and Loren Markee were present. Do you remember that transaction, or that stockholders meeting?

A. No, I can't remember the details. I can't remember it.

Q. All right. I am going to refer you to the second page of the minutes of that meeting, the last full paragraph, in which it says: "It was moved and seconded that the president and secretary of the Rand Truck Line, Inc., together with the vice-president, borrow from Callie B. Heider, on assignment from Mrs. R. R. Rand, the sum of \$43,560.00, payable principal and interest in the sum of \$1,000.00 each and every month, beginning November 1, 1944, until the full amount due on said loan has been fully paid, and said three principal officers of the said [17] corporation are authorized to execute any documents, mortgages, notes, assignments, transfer of the property, assets, rights, stock, and all other interest of the said corporation, and which mortgage and pledge to remain in full force and effect until said borrowings have been fully liquidated."

A. No, I don't remember it. Twelve years is a long time to remember all the details. There's been a lot of water under the bridge.

Q. Was that money that Mr. Heider paid to

(Testimony of Robert R. Rand.)

you, that \$32,000, you say? Was that what was received for the execution of this mortgage?

A. No, there was \$40,000 received.

Q. Well, then, \$40,000, the money that you got for this stock, was what was given for that mortgage, is that right?

A. Well, that satisfied my claim to all the stock.

Q. Now in addition did the corporation receive anything for that mortgage?

A. Well, after I ceased to be president of the corporation I couldn't answer that. While I was president of the corporation, no.

Q. Did you discuss this mortgage with Mr. Heider and Mr. Markee?

A. No, I actually didn't ever know there was a mortgage existed.

Q. Do you remember going to that directors' meeting when you were all supposed to be present?

A. No, I don't.

Q. Do you know whether it was actually held or not? [18]

A. It would be difficult for me follow through all the details of that transaction. I couldn't say. I wouldn't want to say "yes" or "no." I would just rather leave it. Twelve years is a long time.

Q. Well, let's put it this way. As far as you know the corporation received nothing in return for giving this mortgage, is that right?

A. No, I couldn't say that.

Q. Well, what did it receive?

(Testimony of Robert R. Rand.)

A. Well, as far as I know, as I already stated, I don't recognize that note and mortgage.

Q. Well, was there some other contract in existence?

A. I wouldn't say I never had it because I handled a lot of money, and a lot of papers on the various deals. As long as the matter was closed, I proceeded to forget it, because I had a lot of other things to think about, but to the best of my knowledge I never remember of seeing that note. I couldn't say I never saw that note but I don't remember seeing that note, but it could be possible that it was in existence and that I held it. I wouldn't say that I didn't.

Q. Have you had very many transactions of this size in your life, Mr. Rand, involving yourself personally?

A. Well, quite a lot. This was about the largest I have had but I have handled many 25—and \$30,000 transactions, and I have been used to handling considerable money all my life. [19]

Q. You knew what the sense of an endorsement, "Without liability" would be, then, did you not?

A. No, I don't know.

Mr. Dougherty: If the Court please, I object to it. This witness did not make the endorsement. He is being asked about a third person's endorsement and asked to guess what might have occasioned it.

Mr. Bollenback: I am not asking that. I am just asking him if he knew then.

A. No, I don't know.

(Testimony of Robert R. Rand.)

Q. You don't know?

A. It would be absolutely void, according to what Webster's dictionary would say about it. It would be void.

Mr. Bollenback: For the present we have no further questions, your Honor. I would like to keep the witness here, though.

### Cross-Examination

By Mr. Dougherty:

Q. Mr. Rand, what was the condition of the Rand Truck Line when you sold your interest to the Markees? Was it solvent? A. Yes, it was.

Q. Was it on a cash basis?

A. It was entirely on a cash basis. It had no obligations or judgments or any claims against it that I know of, other than the current bills.

Q. This matter of financing between the Markees and Mr. Heider, [20] you knew that there was some financing arrangement?

A. I knew that, yes, sir.

Q. Did you know the details of it?

A. No, I did not. It was of no interest to me as long as I received my money for my stock. I had no further interest, except we remained friendly with them and wished them a great deal of success in the operation of the business.

Q. Do you know whether or not the business continued in a good solvent state for some time?

Mr. Bollenback: I am going to object to that.



(Testimony of Robert R. Rand.)

The witness severed his connections. He has no knowledge.

Mr. Dougherty: I asked him if he knew.

The Referee: He may answer if he knew.

A. I knew nothing about it whatever. I lost contact completely with the organization.

Mr. Dougherty: No further inquiries.

The Referee: Do you have something?

Mr. Bollenback: I don't think so but I would like to ask the witness to remain in the courtroom.

The Referee: May I ask one question? You mentioned that Mr. Heider prepared a contract between you and Vern Markee, whereby you agreed to sell and he agreed to purchase your stock in the Rand Truck Line. Was there such a contract?

A. I can't tell you whether there was, other than a verbal contract, or not. I can't tell you whether there was a written [21] contract or not because I held the checks and I held the stock and I had ample security for money owed to me and that was the main thing I was interested in, and I can't say whether there was any written contract or not.

The Referee: You don't have any such contract in your possession?

A. No, I don't. I don't have any of the papers at all.

Mr. Dougherty: May I ask one or two further questions, your Honor?

(Testimony of Robert R. Rand.)

Further Cross-Examination

By Mr. Dougherty:

Q. Mr. Rand, of course this was a corporation, but you mentioned when Mr. Markee became one of the partners.

A. Well, I meant a stockholder in the corporation. I wish to correct that.

Q. But, in fact, in your operations did you conduct it as a——

Mr. Bollenback (Interrupting): I object to that, your Honor. That isn't proper. It was, in fact, a corporation, and if they conducted it as a partnership it just meant it wasn't operated properly.

Mr. Dougherty: That is a conclusion. I think that the circumstances of how the business was conducted and how it was considered by the owners is of considerable importance.

The Referee: Who was the stockholder you were referring to?

Mr. Dougherty: Mr. Rand, I believe, testified that Mr. Markee [22] acquired an interest, and just as a manner of speaking, I believe Mr. Rand said "when he became one of the partners."

The Referee: How long had he been in there before you sold out.

A. About twenty-three years.

The Referee: Markee had?

A. No, no, no. No, Markee had——

(Testimony of Robert R. Rand.)

The Referee: Well, how long had Markee been in there before you sold out?

A. I couldn't say; just a matter of months.

The Referee: Well, if you want an answer he may answer.

Q. (By Mr. Dougherty): Did you run your business, Mr. Rand, generally as any closely held business is run?

Mr. Bollenback: Oh, if your Honor please, that is a different question entirely. That isn't the question he asked. That is calling for a conclusion and calling for everything else. How does this witness know how "any closely held business is run?"

The Referee: Well, I don't think it is going to be very relevant, one way or the other. Mr. Markee had been in only a few months, and before that, as I understand, Mr. Rand and his sister-in-law were the sole owners of the corporation, is that right?

A. Well, Mrs. Rand, myself and Mrs. Potts held all of the stock.

The Referee: Was she your sister-in-law, Mrs. Potts—did I understand that correctly? [23]

A. She was the wife of a former partner, when I operated it as a partnership, and he died and she inherited his interest in the truck line.

The Referee: I got the impression she was a relative of yours. Am I mistaken?

A. Yes, that's right. It was all in the family.

The Referee: Mr. Dougherty, you had better repeat your question if you want it answered.

(Testimony of Robert R. Rand.)

Mr. Dougherty: Let me ask another question, if I may.

Q. When you sold out, Mr. Rand, did you consider that you were selling out all of the assets of the business? Were you selling the business as a whole to the Markees?

A. I was selling the entire stock in the corporation, which would include all the assets.

The Referee: You held the stock until you got all of your money, didn't you?

A. Yes, I did.

Mr. Bollenback: Are you through, your Honor?

Mr. Rand, since you have been on the stand we have been in touch with Mrs. Rand and she has agreed to come in here this afternoon but she wants you to go out and pick her up. Will you do that and be down here for this afternoon's hearing? I thought that you knew all about this transaction. Of course, technically it is her signature, so as I say, we have asked her to come down, and will you go and pick her up? [24]

Mr. Rand: Well, if the Court would request me and would feel that it was absolutely necessary I would say I would, but I would rather not because Mrs. Rand isn't well. She has high blood pressure and she isn't in a condition to appear here for questioning, but if it is absolutely compulsory it could be done. I don't think—well, it is not my opinion at all. I am speaking out of turn.

Mr. Bollenback: No, you aren't speaking out of turn, because our situation is this, Mr. Rand. As I say, I felt you knew about this transaction and

(Testimony of Robert R. Rand.)

you say now you didn't, and it is her signature and of course, if we are forced to we can subpoena her as we did you.

Mr. Rand: I have already made my statement. If the Court feels it is necessary that she be brought in as a witness, I will.

Mr. Dougherty: If the Court please, the document shows on its face that it was issued to Mrs. Rand, and Mrs. Rand signed it, and counsel has assumed that Mr. Rand might know about it. He had no basis for that assumption. The matter has been going on for some seven years. He has had adequate time to prepare it. I don't know that it is of any particular materiality to Mr. Heider, but I don't see why last-minute subpoenas should be issued in the middle of the examination.

The Referee: This note was made to Mrs. Rand. Was the mortgage made to Mrs. Rand?

Mr. Bollenback: Your Honor, it is apparent on the face of it [25] that this document originally was prepared to be given to Mr. Rand, and you will note particularly on the first mortgage, the title "Mrs." is inserted. You can see on the front page of the mortgage, toward the top, there is even a diagonal bar put in and the "Mrs." inserted, so the transaction was, in fact, supposed to be one with Mr. Rand, but——

The Referee: Well, who assigned the mortgage to Mr. Heider?

Mr. Bollenback: Well, the note is assigned by Mrs. Rand, so I assume she did.

(Testimony of Robert R. Rand.)

The Referee: I thought we might hurry it up if Mr. Rand may have joined in the assignment of the mortgage. It was assigned, wasn't it, Mr. Dougherty?

Mr. Dougherty: Yes, sir.

The Referee: Well, this Exhibit 6, previously received—was that the original mortgage?

Mr. Bollenback: I think that is a copy, your Honor. Well, that is the first mortgage. It might be a duplicate original.

The Referee: Couldn't we have the original mortgage introduced in evidence? To support Mr. Heider's claim it should be in.

Mr. Bollenback: Technically his claim is on the second mortgage, your Honor, but the first mortgage is directly involved because it was never paid in full.

Mr. Miller: Mark these Trustee's Exhibits 14 and 15.

(Thereupon, a sheaf of papers headed "Schedule 100. Comparative Balance Sheet Statement" was marked [26] for identification Trustee's Exhibit No. 14. A certified photostatic copy of the Articles of Incorporation of Rand Truck Line, Inc. was marked for identification Trustee's Exhibit No. 15.)

The Referee: Do you think it is attached to the claim, Mr. Heider?

Mr. Heider: I thought it was attached to the claim, your Honor.

(Testimony of Robert R. Rand.)

Mr. Bollenback: I think that is the second mortgage that is attached to the claim, your Honor. Claim No. 63. It is filed numerically.

Well, Mr. Rand, getting back to the presence of Mrs. Rand here, unless you agree to have her present in court this afternoon it will be necessary for us to cause a subpoena to be issued.

Mr. Rand: Well, I wouldn't be a party to making that necessary. I will co-operate as far as I can.

Mr. Bollenback: Will you agree to have her here? We will try to not upset her, but will you agree to have her here at the commencement of the afternoon hearing?

Mr. Rand: Uh huh.

Mr. Dougherty: We renew our objections, your Honor.

The Referee: Objections to what?

Mr. Dougherty: Objection to calling the witness at this late date. There is a perfectly orderly procedure for subpoenaing [27] witnesses, and when the documentary evidence is as clear as it is here there is no reason for the witness not being called in long ago.

Mr. Bollenback: I am sure Mr. Dougherty objects to this entire transaction.

You are excused, Mr. Rand. Take a seat over here.

(Witness excused.)

Mr. Bollenback: At this time, your Honor, I would like to offer into evidence Trustee's Exhibit

14 for identification, which appears to be photostatic copies of balance sheets of the corporation filed with the Public Utilities Commission of the State of Oregon for the years 1944, '45, '46, '47 and '48.

Mr. Dougherty: We have no objection to Trustee's Exhibit No. 14 being received, subject to this comment: These documents are not, I believe, self-explanatory. Accordingly, we are willing to agree that they are photostatic copies of the balance sheets which were filed; whether or not they are correct, whether or not they were self-explanatory, we doubt. I would invite the Court's attention to the fact, however, that they show an excess of current assets over current liabilities for the time here involved.

Mr. Bollenback: The only comment I have on that is that the record already in evidence on that transaction was that this mortgage involved was never set up on the books, for about three years. [28]

The Referee: It may be received.

Mr. Bollenback: Now at this time I wish to offer Trustee's Exhibit 15 for identification, which purports to be a photostatic copy obtained from the Corporation Commissioner of the Articles of Incorporation of the Rand Truck Line.

Mr. Dougherty: No objection.

The Referee: It may be received.

(Thereupon, the documents heretofore marked Trustee's Exhibit No. 14 and Trustee's Exhibit



No. 15, respectively were marked as received in evidence.)

Mr. Bollenback: Call Vern Markee.

The Referee: Your name is Vern Markee?

Vern Markee: Yes, sir.

### VERN MARKEE

was thereupon produced as a witness in behalf of the Trustee and, being first duly sworn, was examined and testified as follows:

#### Direct Examination

By Mr. Bollenback:

Q. Mr. Markee, it is a fact, is it not, that on or about December 27, 1943 you bought 500 shares of corporate stock of the Rand Truck Line, and in return for that you turned in certain equipment that you had owned? Is that right. A. Yes.

Q. And subsequently during the year 1945 you negotiated for the outstanding stock which was held by Mrs. Potts and the Rands, is that correct?

A. Yes, that's right. [29]

The Referee: Is that '45 or '44?

Mr. Bollenback: Pardon me. It was '44, wasn't it? A. Yes.

Q. And did you agree to pay the Rands \$40,000 for that stock, is that correct? A. Yes.

Q. How were you going to pay for that stock? (Pause.) Let me rephrase my question. When did you first talk to Mr. Heider about this deal?

(Testimony of Vern Markee.)

A. After we had made arrangements with Bob Rand to buy out his interest.

Q. Buy his stock? A. Yes.

Q. It was before the deal was closed?

A. Yes.

Q. And was Heider going to furnish the money to pay for the stock? A. Yes.

Q. And did Mr. Heider know what the transaction was—that it was a purchase of the corporate stock from Rand? A. I believe so, yes.

Q. Well, you explained the deal to him when you went down there, didn't you?

A. Yes, I told him we were buying the stock.

Q. Now Loren Markee, your brother, did furnish \$5,000 of the money, didn't he? [30]

A. That's right.

Q. Mr. Rand has testified that he got \$8,000 at the time the deal was closed. Where did the other three come from?

A. As to that, I can't say. I don't know.

Q. Did you furnish it? A. No, sir.

Q. You didn't put any money up at that time, did you? A. No.

Q. And who else would be interestd in putting money up beside you and Loren? A. No one.

Q. Well, did Otto Heider put this three thousand up? A. I don't know.

Q. Did the corporation pay any money to Bob Rand and Potts? A. No, not that I know of.

Q. Now the payments that were made on this first mortgage, those payments were made from cor-

(Testimony of Vern Markee.)

porate funds, were they not?      A. Yes.

Q. A part of which went through the books of the corporation and part did not, is that correct?

A. That's right.

Q. Part of which was paid to Mr. Heider by cash and part by corporate check, is that right?

A. That's right.

Q. Was Otto Heider ever your attorney? Did he ever handle any [31] legal work for you?

A. Not that I know of.

Q. Now, Mr. Markee, going to a different field, I have a note and mortgage here—I thought it was marked but it isn't—a mortgage from you to the Rand Truck Line, in the amount of \$5,000—for \$5,400, rather, and covering a wood van body with a 3-speed Brownie with 5 speeds. Do you know what that piece of equipment was? (Pause) And a note payable to the Rand Truck Line, signed by you, which was endorsed. Do you remember that transaction? That was turned over to Otto Heider?

Mr. Dougherty: May I inquire who is doing the testifying here?

Mr. Bollenback: You may inquire.

Mr. Dougherty: Three questions have been asked the witness and he hasn't been given an opportunity to answer any of them.

A. This particular piece of equipment is a Sterling truck and van body used by the Rand Truck Lines, but I don't follow exactly what happened here.

Q. (By Mr. Bollenback): Well, I am going to

(Testimony of Vern Markee.)

ask you to remember at that time whether or not you borrowed any money from Otto Heider?

A. Yes.

Q. And do you remember how much you borrowed from him?

A. According to this note it was \$5,400.

Mr. Bollenback: I think probably that should be marked. I [32] thought it was marked at a previous hearing, but apparently it wasn't.

Q. I am going to hand you a check for \$5,000, payable to Vern Markee and Rand Truck Line, dated November 2, 1945, and ask you whether that is what you received for that mortgage?

A. Yes, that is the check we received.

Mr. Dougherty: Your Honor, I fail to see any relevancy here at all.

The Referee: What is the date of those instruments?

Mr. Dougherty: This is November 2, 1945.

Mr. Bollenback: The note is in October and the check is in November.

Mr. Dougherty: Yes. I thought they were talking about a transaction which occurred in August of '46.

The Referee: I think we had better clear up the original transactions by having the original mortgage of 1944. The original mortgage of 1946 is attached to Mr. Heider's claim.

Mr. Bollenback: Do you, your Honor, want an explanation of what I have in mind at this time?

The Referee: All right.

(Testimony of Vern Markee.)

Mr. Bollenback: And it is a matter which I think Mr. Heider is going to be bound to prove.

At the hearing that we had, Mr. Heider produced checks totaling \$36,500, which includes this \$5,000 check and it was his claim at that time that these checks represented the money [33] that he paid out on this first mortgage. At this stage of the proceeding we have Mr. Rand, who says he got \$3,000 which nobody knows where it came from, and we also have testimony by Mr. Markee that this \$5,000 check that is claimed to be part of the consideration for the first mortgage is, in fact, a consideration for one of these subordinate mortgages which were paid off by the second mortgage, so we find Mr. Heider here who has only produced \$31,500 worth of checks for a \$43,000 mortgage.

The Referee: Well, you have those marked.

Mr. Bollenback: Very well. The check itself——

The Referee: Has it been marked?

Mr. Bollenback: It hasn't been marked, your Honor.

Mr. Dougherty: If the Court please, of course by remaining silent we don't agree to counsel's misstatement of the record. The statement was that cash and checks were delivered.

The Referee: Do you mean formerly?

Mr. Dougherty: Yes, sir.

(Thereupon, a check dated November 2, 1945, drawn on The First National Bank of Sheridan, in favor of Vern Markee and Rand Truck Line,

(Testimony of Vern Markee.)

in the amount of \$5,000, signed by Otto W. Heider, was marked for identification Trustee's Exhibit No. 16.

A promissory note in the amount of \$5,400, dated at Sheridan, Oregon, October 31, 1945, in favor of Rand Truck Line, signed by Vern Markee, attached to [34] a chattel mortgage of even date and amount, in favor of Rand Truck Line, signed by Vern Markee, was marked for identification Trustee's Exhibit No. 17.)

Mr. Bollenback: At this time, your Honor, Trustee's Exhibit 16 is the \$5,000 check referred to; Trustee's Exhibit 17 is the note and mortgage which were just referred to.

The Referee: You are offering them now?

Mr. Bollenback: I am offering them in evidence.

Mr. Dougherty: We have no objection to the exhibits being received.

The Referee: They may be received.

(Thereupon, the check heretofore marked Trustee's Exhibit No. 16, and the note and mortgage heretofore marked Trustee's Exhibit No. 17 were marked as received in evidence.)

Mr. Bollenback: Now, if the Court please, may we offer in evidence at this time not only the Heider testimony at the previous hearing, but also the testimony of Vern Markee, which was given July 6, 1949? It is all bound in the same transcript and we

(Testimony of Vern Markee.)

feel that that should be part of the evidence in this case too.

Mr. Dougherty: I am sorry, your Honor. We will have to object. It relates to matters not germane to this controversy, in a large part. Mr. Markee is in court. [35]

Mr. Bollenback: We will accept the modification that it will be considered as evidence only insofar as it would be relevant.

Mr. Dougherty: I haven't examined it, your Honor, and I am not prepared blindly to stipulate that it may be received, and I do believe that it is subject to an objection for relevancy.

Mr. Bollenback: I have no further questions, Mr. Markee.

#### Cross-Examination

By Mr. Dougherty:

Q. Mr. Markee, when you went into Rand Truck Line, was it a solvent company, operating on a cash basis? A. At the time I went in?

Q. Yes. A. Yes, I am sure it was.

Q. And at the time of these various transactions with Mr. Heider was it a good, going business, operating on a cash basis?

A. Which transactions are you referring to now?

Q. Well, for example, when this money was borrowed and there was a Rand Truck Line mortgage assigned to Mr. Heider.

A. The first mortgage or second mortgage?

Q. First mortgage. A. Yes, it was.

(Testimony of Vern Markee.)

Q. Did you ever discuss the internal affairs of the corporation with Mr. Heider?

A. No, sir, I didn't believe I did.

Q. Do you think that any of the other stockholders or officers, [36] or do you know whether or not any of the stockholders or officers discussed the internal affairs of the corporation with Mr. Heider?

A. I can't speak for the other stockholders.

Q. To your knowledge did any of the others ever discuss the internal affairs with him?

A. I can't say; I am sorry. They might have.

Q. They might have, but do you know of any occasion when they did? Do you know of any time when they did?

A. I wouldn't know of any particular time but they probably did discuss it with Mr. Heider.

Q. You did not do so? A. No.

Q. It is a fact that there were various financial transactions through Mr. Heider's office?

A. Yes.

Mr. Dougherty: I have no further questions.

Mr. Bollenback: Will the reporter read the last question, please?

(The last question was read.)

The Referee: Did the corporation have any difficulty in meeting these payments of a thousand dollars every month throughout that whole time?

A. Yes, sir.

The Referee: Did you have to refinance in '46?

A. Yes, sir. I am not sure of the date, sir, but we did. [37]



(Testimony of Vern Markee.)

The Referee: That is what you call the second mortgage?

A. I think so.

The Referee: Why did you have to refinance at that time? Were you having difficulties?

A. Yes. I would have to look over the details at the time to remember exactly what happened, but we were having troubles at that time.

The Referee: Didn't you buy some additional equipment at that time, or did you, at the time of the second mortgage?

A. I can't say for sure.

### Redirect Examination

By Mr. Bollenback:

Q. Well, Mr. Markee, actually you had to borrow money from Mr. Heider practically immediately, didn't you? Not only did you have that mortgage that we were talking about awhile ago, but I will hand you Trustee's Exhibit 4, which was a mortgage that was signed in 1946. That was another occasion where you got some money from Mr. Heider, wasn't it?

Mr. Dougherty: May the record show that the note that has been handed the witness is signed by Rand Truck Line and that Mr. Markee's name nor signature appears on it.

Do I understand counsel that when you say "you" you meant Rand Truck Line?

(Testimony of Vern Markee.)

Mr. Bollenback: I meant Rand Truck Line. They were in financial difficulties. [38]

A. This note and mortgage was signed by H. H. Macy, at that time general manager, and I did know of it but I didn't participate in this particular note myself.

Q. Now I am going to hand you——

The Referee: Just a minute. You will have to dispose of these matters. You referred to an exhibit. Is it understood that all of the exhibits under the former record are to be introduced in evidence?

Mr. Bollenback: It is my understanding that that was what the stipulation was.

Mr. Dougherty: I understood we had a stipulation concerning Mr. Heider's prior testimony. We have no objection to any exhibits being received which were previously received and which relate to Mr. Heider in any way. In view of the fact that this particular instrument is payable to the order of Earl Walden and relates to the purchase of a Ford van, and is not negotiated to Mr. Heider, and was not assigned to him, at the moment I don't see any connection with Mr. Heider. There may be.

Mr. Bollenback: Mr. Dougherty, if you will refer to the mortgage you will find that Mr. Heider was made an alternate payee.

Mr. Dougherty: It says, “\* \* \* whereas Rand Truck Line, by H. H. Macy, Gen. Mgr. \* \* \* has purchased from Earl Walden or Otto W. Heider \* \* \*” a certain Ford van for a price of \$1,080.00. Well,

(Testimony of Vern Markee.)

there is that connection, for whatever it may be worth.

The Referee: It may be received. [39]

(Thereupon, the note and mortgage hereinbefore described, previously marked Trustee's Exhibit 4 in the former hearing, was marked as received in evidence.)

Mr. Bollenback: Will you mark this?

(Thereupon, a document entitled "Conditional Sales Contract," executed by Rand Truck Line, Vern Markee, dated April 9, 1946, and covering one 1945 Fruehauf van semi-trailer, with a promissory note in the amount of \$2,700.00, of even date and like signature, in favor of Otto W. Heider attached as a part thereof, was marked for identification Trustee's Exhibit No. 18.)

Q. (By Mr. Bollenback): Now, Mr. Markee, I hand you Trustee's Exhibit 18 for identification, which purports to be a conditional sales contract, with a note attached, signed by Rand Truck Line, payable to Otto W. Heider, dated April 9, 1946, and ask you whether or not that isn't also a part of the financing that the Rand Truck Line was forced to do?

A. Yes, this was purchase of additional equipment to be used in the operation.

Mr. Dougherty: No objection.

(Testimony of Vern Markee.)

The Referee. Was that purchased from Mr. Heider?

A. No, sir, I think it was from Fruehauf Trailers, in Portland.

The Referee: It may be received.

(Thereupon, the document hereinbefore marked Trustee's [40] Exhibit 18 was marked as received in evidence.)

Mr. Bollenback: I have nothing further at this time.

#### Recross-Examination

By Mr. Dougherty:

Q. Mr. Markee, when did you suffer your large fire loss?

A. Either '46 or '48; I am not sure as to the date.

Q. Was it that unexpected fire loss which was the immediate cause of the financial difficulties of the corporation?

Mr. Bollenback: Object to that as calling for a conclusion.

The Referee: Overruled.

A. Well, I can't say as to how much damage it did but it was quite a drain on the operation of the truck line, yes.

Q. Some of these other financing arrangements where Rand Truck Line bought equipment and borrowed money from Mr. Heider to buy the equipment and gave him a chattel mortgage, or possibly even

(Testimony of Vern Markee.)

bought equipment from him on a conditional sales contract, were there several of those transactions?

A. Yes, during the number of years there was.

Q. And were some of those prior conditional sales contracts or chattel mortgages and the obligations evidenced by them included in what we refer to as the second mortgage?

A. I can't answer to that; I don't know. If I did answer I would be just guessing.

Mr. Dougherty: No further inquiries. [41]

#### Further Redirect Examination

By Mr. Bollenback:

Q. Mr. Markee, were those fire loss claims ever paid?

A. I can't answer that either, because I didn't have anything to do with it.

Q. Well, I think your fire occurred in 1946, didn't it? A. Somewheres around there, yes.

Mr. Bollenback: I wonder if I might have Claim No. 2, your Honor?

Mark this, please.

(Thereupon, a document headed "Proof of Claim in Bankruptcy," signed by Gladys Aljovin on behalf of Better Products Co., together with supporting documents attached, was marked for identification Trustee's Exhibit No. 19.)

Mr. Bollenback: At this time I would like to offer in evidence Trustee's Exhibit No. 19, which

purports to be a claim filed herein by Better Products Co., resulting from a loss from fire in the terminal in McMinnville, supported by a bill of lading dated July 15, 1946, and also supported by a letter signed by Beryl B. Taylor, President of the Rand Truck Line, Inc., dated April 1, 1948, in which they acknowledge the indebtedness of \$53.00 growing out of the fire in McMinnville on July 18, 1946.

The Referee: The purpose of the offer?

Mr. Bollenback: The purpose of the offer is not only to establish a creditor that has existed up to the present time, [42] from that date, but also to fix the date of the fire.

Mr. Dougherty: If the Court please, the offered exhibit is in this connection purely hearsay. Now if the witness can refresh his recollection from this, or something, we have no objection to that.

The Referee: I think it may be received. When those proofs of claim import validity on their face they are admissible in evidence as prima facie evidence of the claim itself, and it has just been put in for two purposes, so I will overrule the objection. It may be received.

(Thereupon, the document heretofore marked Trustee's Exhibit No. 19 was marked as received in evidence.)

Mr. Bollenback: We have nothing further of Mr. Markee.

Mr. Dougherty: No further inquiries.

(Witness excused.)

Mr. Bollenback: Your Honor, we have Mrs. Rand coming in this afternoon, and also one other witness who will be very short, and we have nothing further to occupy the morning with. We think we have made a prima facie case but we do want to reserve the right to call the witnesses.

The Referee: What is your pleasure, Mr. Dougherty? Would you like to adjourn now until two and consider this matter, or would you like to proceed with any evidence you want to introduce?

Mr. Dougherty: If the Court please, we do not wish to proceed at this time, primarily because we feel that nothing approaching [43] a prima facie case has been made.

We would like at this time to be sure, in line with the Court's prior comments, that the proper documents are in evidence with respect to the Proof of Claim.

I have here what purports to be a recorded mortgage from Rand Truck Line to H. H. Macy, bearing the County Clerk's stamp.

The Referee: What is the date of that?

Mr. Dougherty: It is dated August 7, 1946.

Mr. Miller: Is there a file number on that, Mr. Dougherty?

Mr. Dougherty: It is Volume 107, page 676 of the Mortgage Records of Yamhill County.

The Referee: I would like to have that added as an exhibit in support of your claim, because the claim has been questioned and I would like to have you support it by the documents. He did attach to

his Proof of Secured Claim what seems to be a duplicate original, but not the recorded one.

Mr. Dougherty: May we so offer it now?

The Referee: Yes.

Will you mark that exhibit?

(Thereupon, the mortgage hereinabove described was marked for identification as Claimant's Exhibit No. 20.)

Mr. Dougherty: Has this been received, your Honor?

The Referee: It may be received, yes. [44]

(Thereupon, the document heretofore marked Claimant's Exhibit No. 20 was marked as received in evidence.)

Mr. Dougherty: May I inquire whether or not the assignment appears with the Proof of Claim?

The Referee: Suppose you look at it.

Mr. Dougherty: If the Court please, the assignment does not seem to be attached to the claim. May I inquire of counsel whether or not any objection is made? Well, as a matter of fact we know it isn't because it isn't in the objections to the Proof of Claim. No objection is taken on that ground. I would like to have an opportunity to attach it to the original.

The Referee: Could we have the original mortgage in 1944, because I think this is a renewal of at least part of the mortgage of '44.

Mr. Heider: I didn't know the old mortgage was involved and I kind of doubt if I brought it along.



The Referee: You did introduce at the former hearing a copy of it.

Mr. Heider: You say a copy was introduced?

The Referee: A copy was introduced.

Mr. Heider: Then I think the original mortgage of 1944 has been returned to Rand Truck Line and would not be in our possession.

The Referee: Do you have the original mortgage?

Mr. Bollenback: The only one I have, your Honor, is the one put in evidence here, which apparently was a signed copy, all [45] right. There is no filing on it.

Mr. Heider: If it was recorded I could get a certified copy of it and have it sent down.

The Referee: That would suffice. Do they photostat now?

Mr. Heider: Oh, yes, they photostat. I would be very glad to.

Mr. Miller: Mr. Dougherty, I have examined Claimant's Exhibit No. 20 and I wonder if you could answer some questions. It contains both real and personal property and it states on its back that it is recorded in Book 107, page 676, Record of Mortgages of said county. I would like to ask if you know, was that recorded in the real property mortgages or in the personal property mortgages?

Mr. Dougherty: It is cross-indexed as the statute provides.

Mr. Miller: They usually say so on the mortgage. I find no such statement here is why I am asking.

Mr. Dougherty: I don't believe they do so in Yamhill County, however.

Mr. Miller: Then I would like to ask Mr. Heider unofficially if he knows, was this particular mortgage the mortgage of August 7, 1946, recorded in Multnomah or any other county except Yamhill?

Mr. Heider: No, except the Register of Migratory Chattels in the Secretary of State's office.

Mr. Miller: Was that a filing of the entire mortgage in the Migratory Chattels records, or just the vehicles?

Mr. Heider: No, just the vehicles record was made in Salem. [46]

Mr. Miller: Can you answer me about the first mortgage now? There seemed to be some doubt at the first meeting about this.

Mr. Heider: I think the same filing on that was made as on this in Yamhill County, and I can get a certified copy of it.

The Referee: He has agreed to get us a certified photostatic copy of that mortgage.

Mr. Heider: It will have the filings on it.

The Referee: Well, it is nearly ten minutes till twelve. We will adjourn this hearing, to reconvene at two o'clock. The witnesses under subpoena will please return at two o'clock.

(Noon recess.) [47]

Afternoon Session, 2:00 P.M.

The Referee: You may proceed.

Mr. Bollenback: I will call Mr. Ellis, please.

DEAN ELLIS

was thereupon produced as a witness in behalf of the Trustee and, being first duly sworn, was examined and testified as follows:

Direct Examination

By Mr. Miller:

Q. What is your occupation, Mr. Ellis?

A. I am a lawyer.

Q. And how do you practice law? Are you in a partnership?

A. I am in a partnership with my father, William P. Ellis.

Q. Now did the partnership represent, at any time, Rand Truck Line? A. Yes, it did.

Q. Is Rand Truck Line indebted to the partnership? A. Yes, it is.

Q. Have you a statement of the indebtedness of Rand Truck Line to the partnership of Ellis & Ellis? A. Yes, I have.

Q. May we have it, please?

We will ask that this document be marked for identification as Trustee's Exhibit 21.

(Thereupon, a statement of Ellis & Ellis to Rand Truck [48] Lines, Inc., dated July 8, 1949, was marked for identification Trustee's Exhibit No. 21.)

Q. Now is the sum shown here——

Mr. Dougherty: We object to it, your Honor, because no relevancy with respect to the instant proceeding has been shown.

(Testimony of Dean Ellis.)

Mr. Miller: I haven't offered it yet.

Mr. Dougherty: Well, don't ask him any questions about it until you do, please.

Mr. Miller: That is my privilege.

Q. This sum shown on it, \$1,099.67, is still unpaid, is it?

Mr. Dougherty: Objected to.

The Referee: He may answer.

A. It hasn't been paid.

Q. (By Mr. Miller): And did Ellis & Ellis file a claim in this proceeding?

A. Yes, they did.

Mr. Miller: I will offer it.

Mr. Dougherty: Objected to on the ground that it is irrelevant with respect to the claim of Otto W. Heider, which we understood was the matter being considered today.

Mr. Miller: Well, the matter is to show, your Honor, that there was a creditor who had rights under the Oregon law against this mortgage.

The Referee: When did you say it was performed?

Mr. Miller: That is stated on the face of it. I haven't [49] finished with the witness yet.

The Referee: All right.

Q. William P. Ellis was engaged in the practice of law as an individual prior to the formation of this partnership? A. That is correct.

Q. And are the books and records of William P. Ellis in the office which you now occupy?

A. Yes.

(Testimony of Dean Ellis.)

Q. Are you familiar with the books and records of William P. Ellis? A. I am.

Q. Do they show an indebtedness from Rand Truck Line to William P. Ellis? A. Yes.

Q. And is that a copy of the indebtedness there?

A. That is a copy of the indebtedness.

Mr. Miller: We will ask that this be marked Trustee's next exhibit.

(Thereupon, a statement of Wm. P. Ellis, Individual, to Rand Truck Lines, Inc., dated July 8, 1949, was marked for identification Trustee's Exhibit No. 22.)

Q. And to your knowledge is this indebtedness on Trustee's Exhibit 22, \$1,686.00, still unpaid?

A. It has not been paid.

Mr. Miller: We will offer Trustee's Exhibits Nos. 21 and 22, [50] your Honor, two pages, to show the existence of a creditor from '46 prior to the existence of the mortgage, right on through.

Mr. Dougherty: Objected to on the ground of relevancy and because the documents do not show or purport to show what counsel has stated for them. They show accounts and indebtedness as of July 8, 1949, subsequent to the mortgages.

Mr. Miller: If the Court please, counsel is not reading from the documents. He is summarizing. May I see the document, please? Part of the services were rendered August 1, 1946, according to the document.

Mr. Dougherty. There is an item for services

(Testimony of Dean Ellis.)

rendered between August 1, 1946, and August 1, 1948, which is some time subsequent to the priority claim here.

Mr. Miller: If the Court please, the interpretation of the document is for the Court. We are offering the documents into evidence with the Court's right, of course, to interpret them as the Court sees fit.

The Referee: You had this witness testify what services were performed?

Mr. Miller: Not that early, your Honor. His father, Mr. Ellis Sr., is out of town.

The Referee: I am going to overrule the objection at this time. They will be received subject to the objection of counsel.

(Thereupon, the documents heretofore marked Trustee's Exhibit No. 21 and Trustee's Exhibit No. 22, respectively, [51] were marked as received in evidence.)

Mr. Miller: No further questions.

### Cross-Examination

By Mr. Dougherty:

Q. Was any security received, Mr. Ellis?

A. There was no security for any of the obligation.

Mr. Dougherty: No further inquiries.

Mr. Miller: Thank you very much.

(Witness excused.)

Mr. Bollenback: Call Mrs. Rand, please.

GOLDA I. RAND

was thereupon produced as a witness in behalf of the Trustee and, being first duly sworn, was examined and testified as follows:

Direct Examination

By Mr. Bollenback:

Q. Now, Mrs. Rand, prior to September 28, 1944, were you a stockholder in the Rand Truck Line?

A. Forty-what?

Q. Forty-four. A. I presume so.

Q. Well, just so it won't confuse you, that was the date, I think, of the transaction in which Vern Markee and his wife and Loren Markee acquired your stock in the Rand Truck Line. Did you have any part in the negotiations going on for the sale of your [52] stock? A. No.

Q. Mr. Rand handled it, is that right?

A. That's right.

Q. The note and mortgage which were given at that time, Mrs. Rand, Trustee's Exhibits 3 and 6, show that that note and mortgage were payable to you. Now was there any discussion with you before that note and mortgage were executed as to your being made payee of that mortgage?

A. No, sir.

Q. You didn't know anything about the transaction?

A. Well, I knew that we were selling out but I didn't have any part in it that I remember of.

(Testimony of Golda I. Rand.)

Q. Your husband said this morning that he thought he was hunting at the time the transaction was closed. A. That's right.

Q. Now is that your signature on the back of that note? A. Yes, it is.

Q. Do you remember where you were when you signed that endorsement?

A. In Mr. Heider's office.

Q. Was there any discussion at that time as to why those typewritten words were above your signature?

A. So far as I am concerned I was asked to go up there and sign whatever papers were necessary to close the deal and I went up and signed them and I never read the note and I don't know anything [53] about it.

Q. The papers were there before you went there, is that right? A. Yes.

Q. You didn't take them with you? A. No.

Q. They were in his office when you got there?

A. I am sure they were.

Q. Leastwise you didn't take them there?

A. No.

Q. And Mr. Heider just put some papers in front of you and asked you to sign them, is that what happened?

A. That must have been what it was, and I trusted him.

Q. Now, Mrs. Rand, did the corporation receive anything for that note and mortgage that it gave you? A. Do you mean before this was signed?



(Testimony of Golda I. Rand.)

Q. No, those papers in front of you, that note and mortgage, are an agreement on the part of the Rand Truck Line to pay you \$43,560, if I have the figures correct. Now, that is what those documents represent. Did you give the Rand Truck Line anything for that note and mortgage? A. Did I?

Q. Yes. A. No, sir.

Q. Do you know if anyone else gave the Rand Truck Line anything for that note and [54] mortgage?

A. Well, who do you mean, anybody else?

Q. Well, you were, up to that time, a stockholder of the corporation, and the corporation executed a note and mortgage for forty-three thousand, five hundred and some odd dollars. Now what did the corporation get in return for that note and mortgage?

A. Well, they got the full payment, as far as I know.

Q. You mean that the money was paid to the corporation? A. Well, it must have been.

Q. Wasn't the money paid to you and Mr. Rand?

A. Well, there was just three in the corporation, my sister-in-law, and Mr. Rand, and myself.

Q. And you three are the ones that got the money, isn't that right?

A. That's right.

Q. And that mortgage was drawn so that Mr. Heider or the Markees would pay you some money in payment of your stock in the corporation; that

(Testimony of Golda I. Rand.)

is what it was, wasn't it?      A. That's true.

Q. And the corporation itself, as distinguished from the stockholders, didn't get anything, did it?

A. That I don't know.

Q. Now who asked you to go to Mr. Heider's office?      A. Mr. Rand.

Q. Mr. Rand. Was the time set for the appointment for you to go or were you supposed to wait until Mr. Heider notified you, or what? [55]

A. That I don't remember. It is a long time ago.

Q. Did you get some money at the time you signed these papers?      A. No, sir.

Q. You just went in and signed them and turned around and walked out?      A. That's right.

Mr. Bollenback: You may inquire.

### Cross-Examination

By Mr. Dougherty:

Q. When you sold out the business and signed these papers, Mrs. Rand, it was a good, going business, wasn't it?      A. Well, yes.

Q. And when you sold it you sold it clean? I mean any bills had been paid except whatever might be quite current, is that right?

A. I don't remember that.

Q. So far as you recall, the company, when you sold it, wasn't indebted at all?

A. I don't think so.

Q. And was it your understanding that you were selling the company and all of its assets?

(Testimony of Golda I. Rand.)

A. I can't answer you that.

Q. This has been how many years ago?

A. Twelve years.

Mr. Dougherty: No further inquiries. [56]

Redirect Examination

By Mr. Bollenback:

Q. You did know, didn't you, Mrs. Rand, that what you were selling was the capital stock in the corporation?

A. I wasn't too familiar with it.

Q. You let your husband take care of that?

A. That's right.

Q. I may be repeating myself, but just to be sure, you didn't yourself personally, pay anything to this corporation when it executed this mortgage in your favor, did you?      A. No.

Mr. Bollenback: I think that is all.

The Referee: Thank you. May Mrs. Rand be excused now?

Mr. Bollenback: I think so, your Honor, and thank you for coming down, Mrs. Rand.

The Referee: And how about Mr. Rand?

Mr. Bollenback: So far as we are concerned you may go, Mr. Rand. Thank you.

The Referee: You are welcome to stay, though.

(Witness excused.)

Mr. Miller: If the Court please, the Trustee offers into evidence the schedules of Rand Truck

(Testimony of Golda I. Rand.)

Line, an Oregon corporation. If necessary we can get Mr. Taylor to identify the signatures.

(Thereupon, a document entitled "Statement of Affairs" [57] and pertaining to Rand Truck Line, Inc., was marked for identification as Trustee's Exhibit No. 23.)

Mr. Dougherty: May I inquire, are the schedules being offered as evidence of the truth of any matters stated in the schedules?

Mr. Miller: The statement of assets and liabilities of the corporation as of the date of bankruptcy—that is, the corporation's statement of it. It is rebuttable, of course.

Mr. Dougherty: We have no objection to the schedules being considered as the statement of the person who prepared them, no.

The Referee: They may be received.

(Thereupon, the document heretofore marked Trustee's Exhibit No. 23 was marked as received in evidence.)

Mr. Miller: If the Court please, the Trustee offers into evidence the claims filed here by creditors, numbers 1 to 114, inclusive.

The Referee: As one exhibit?

Mr. Miller: As one exhibit. I might state, your Honor, that I believe Claim 2 is already in evidence, but we will just offer the entire group as one exhibit.

The Referee: Any objection?

Mr. Dougherty: Your Honor, we cannot admit the truth of any matters stated in the claims. We can admit claims have been made under these circumstances and in certain amounts.

The Referee: They are all made under oath of the claimants. They may be received. I am not sure in my mind what relevancy [58] they may have, but I think I should have them in evidence if the briefs of the law indicate that they are matters that should be considered.

Mr. Bollenback: That will be Trustee's Exhibit 24, the claims.

The Referee: Well, you just mark the outside of the file.

(Thereupon, the file containing the above-described claims was marked as received in evidence as Trustee's Exhibit No. 24.)

Mr. Bollenback: Will you mark these?

(Thereupon, a packet of checks drawn by Otto W. Heider on The First National Bank of Sheridan, Nos. 1 to 63 inclusive being in the amount of \$500.00 each, drawn in favor of R. R. Rand and/or Goldie I. Rand, and unnumbered checks to the same payees in the respective sums of \$359.06, \$787.88 and \$33.70, and one check drawn to Rand Truck Line in the sum of \$148.59, by the same payor on the same bank, with adding machine tape attached, was marked for identification as Trustee's Exhibit No. 25.

A packet of 11 receipts signed by Otto W.

Heider and made in favor of Rand Truck Line and in favor of Vern Markee, together with 2 checks drawn on The First National Bank of McMinnville by H. H. Macy in the sum of \$2,500.00 each, one payable to Vern Markee and the other payable to Loren Markee, were [59] marked for identification as Trustee's Exhibit No. 26.

A check drawn on the Douglas County State Bank, Roseburg, Oregon, by Otto W. Heider to Rand Truck Line, in the sum of \$5,000, 2 checks drawn on The First National Bank of Sheridan by Otto W. Heider, one in favor of Rand Truck Line in the sum of \$4,508.00 and the other in favor of Rand Truck Line, Inc., and Transport Bodies & Equipment Co., in the sum of \$3,000, and a charge-your-account slip from the First National Bank, Sheridan, Oregon, to Otto W. Heider, covering a certified check dated August 6, 1946, to Rand Truck Line in the sum of \$5,000.00 were marked for identification as Trustee's Exhibit No. 27. (Adding machine tape attached.)

Mr. Bollenback: At this time I would like to offer into evidence Trustee's Exhibit No. 25 for identification, which is the group of 63 checks of \$500, drawn by Otto Heider, payable to R. R. Rand and/or Golda Rand, together with some other checks by the same drawor and the same payees, bearing notations of interest. There is also one check in here which probably might be irrelevant but I felt it should go in, and that is the check to

Rand Truck Line in the amount of \$148.59. As far as I know, it is for some other transaction, not involved here, but as long as it is Mr. Heider's check and produced here I thought it should go into [60] evidence; either that or be returned to him.

Mr. Dougherty: No objection.

The Referee: It may be received.

(Thereupon, the packet of checks heretofore marked Trustee's Exhibit No. 25 was marked as received in evidence.)

Mr. Bollenback: I shall offer Trustee's Exhibit 26 into evidence, which in fact consists of 11 receipts for various amounts and various dates, signed by Otto Heider. Some of them are made in favor of the Rand Truck Line, some in favor of Vern Markee, and the two checks for \$2500.00 each dated January 12, 1946, signed by H. H. Macy, payable to Vern Markee—one to Vern Markee and one to Loren Markee, both of which checks were endorsed by the payee and bear the subsequent endorsement of Otto Heider.

Mr. Dougherty: No objection.

The Referee: They may be received.

(Thereupon, the packet of receipts and checks heretofore marked Trustee's Exhibit No. 26 was marked as received in evidence.)

Mr. Bollenback: At this time I wish to offer into evidence Trustee's Exhibit 27. The exhibit consists of adding machine tape with items totaling \$36,027.00, with the pen and ink notation immediately

below it, "Plus services," together with a check drawn by Otto Heider on The First National Bank of Sheridan, dated August 14, 1946, payable to the Rand Truck Line for [61] \$4,508.00, together with the check drawn on the Douglas County State Bank of Roseburg, Oregon, by Otto Heider, dated August 7, 1946, payable to Rand Truck Line, in the amount of \$5,000.00; the check on The First National Bank of Sheridan drawn by Otto Heider, payable to the order of Rand Truck Line, Inc., and Transport Bodies & Equipment Co. for \$3,000.00, dated August 7, 1946, bearing on the top of the check a notation, "for title for 1946 Transport Van Trailer," together with a statement of a certified check issued by The First National Bank of Sheridan showing that a certified check dated August 6, 1946, of Otto Heider, payable to Rand Truck Line, in the amount of \$5,000.00 was certified, signed by Frances Papstein, cashier.

It is my understanding that this exhibit shows the claim make-up of the second mortgage.

The Referee: What exhibit is that?

Mr. Bollenback: It is 27, I think, your Honor.

Mr. Dougherty: No objection.

The Referee: It may be received.

(Thereupon, the sheaf of checks and documents heretofore marked Trustee's Exhibit No. 27 was marked as received in evidence.)

The Referee: Any further testimony?

Mr. Miller: We will call the Trustee, Mr. McAllister, please. [62]



S. A. McALLISTER

the Trustee, was thereupon produced as a witness, and, being first duly sworn, was examined and testified as follows:

Direct Examination

By Mr. Miller:

Q. I hand you a document headed "Discount on Capital Stock, Account No. 1900." Do you recognize that? A. Yes, sir.

Q. Did it come from the books and records of the bankrupt? A. It did.

Q. It came from the ledger, did it?

A. General ledger, yes.

Mr. Miller: I will ask that this be marked.

(Thereupon, the ledger sheet above described was marked for identification as Trustee's Exhibit No. 28.)

Q. I am handing you Trustee's Exhibit 28 for identification. Just what is that document?

A. It is a journal entry made on July 31, 1944, setting up a total asset of \$20,732.66, of which amount \$12,500.00 is set up as franchise and permits. The balance, \$8,232.66, is set up as good will.

Q. Well, then those two items together make up the item of Discount on Capital Stock?

A. That's right.

Mr. Miller: That is all. [63]

Mr. Miller: We will offer in evidence Trustee's Exhibit 28 for identification, your Honor.

Mr. Dougherty: We object to it on several

(Testimony of S. A. McAllister.)

grounds. First, the Trustee has indicated no personal knowledge of it; secondly, we very strenuously object to morsels and items being torn out of the books of account and offered piecemeal. Thirdly, we object because there is no connection shown and none in evidence concerning any knowledge which this claimant might have had of any such transaction, and in fact, the three dates, any of the transactions between Mr. Heider and the Rand Truck Line, which are involved here. Fourth, that no relevancy has been shown.

Mr. Miller: If the Court please, at the time that the Trustee offered into evidence Trustee's Exhibit No. 14, being the balance sheets of the bankrupt, counsel for the claimant remarked that there were certain things in there that needed explaining. The offered document, Trustee's Exhibit No. 28 for identification, is a ledger sheet which tends to explain one unexplainable item on Trustee's Exhibit No. 14, the item of Discount on Capital Stock. In other words, it is a direct reference from the balance sheet as shown on Trustee's Exhibit 27 to the ledger of the bankrupt.

Of course, the Trustee has no personal knowledge of the books, except he knows what books were turned over to him by the bankrupt, and he has said these were the books and records of the bankrupt, turned over to him. [64]

As far as taking out part, I will be glad to offer the ledger in toto as a part of the same exhibit. I merely didn't want to incumber the exhibits.

(Testimony of S. A. McAllister.)

As far as the witness' knowledge, when you are proving insolvency that is not improper. We have alleged insolvency and this goes to show insolvency.

We will offer the entire ledger, your Honor, and ask that the entire ledger be marked Trustee's Exhibit 28 and offer it into evidence.

I would like to say one more thing your Honor, as far as these books or any others are concerned, anybody's testimony as to what is in these books would be hearsay. These are the books of original entry and they are the best evidence of the state of the business affairs of the company.

Mr. Dougherty: If the Court please, if counsel is going to make statements of fact of that sort I believe he should be sworn, if he is stating of his own knowledge that this is the book of original entry.

The Referee: I think there are persons in the room that could prove that if he would like to have it.

Mr. Dougherty: May I inquire preliminarily?

The Referee: Yes.

Mr. Dougherty: Mr. McAllister, you have long experience as an accountant, do you not?

A. That is right. [65]

Mr. Dougherty: Mr. McAllister, I hand you Trustee's proffered exhibit for identification No. 28, being not only the one sheet but the entire book, and ask you if it is not the fact that that isn't a book of original entry but simply is a ledger containing part of the balances from other accounts?

(Testimony of S. A. McAllister.)

A. It is a general ledger, is what it is termed. It shows all the expense items, and asset items, and liability and so forth.

Mr. Dougherty: Yes, but it isn't a volume of original entry, is it?

A. There could be some other entries, yes; there would have to be.

Mr. Dougherty: The entry would be on the journal and on the various accounts that this book merely summarizes? A. That's right.

Mr. Dougherty: Do you know why, Mr. McAllister, part of the 1944 sheets are missing from this volume?

A. I think I can explain that. I think possibly Mr. Taylor could explain it better, but it seemed they had a habit every few years of transferring the sheets, and that is what they did.

Mr. Dougherty: So this isn't a complete volume in that respect?

A. It is complete from 1944 through '46.

Mr. Dougherty: Well, aren't some of the '44 sheets missing from there, Mr. McAllister?

A. Well, except this one that is missing, Exhibit No. 28.

Mr. Dougherty: And aren't there 1946 transactions which [66] aren't recorded there?

A. Not to my knowledge. It looks as though some of these accounts have balances as of January 1, 1946. They aren't itemized and I think you are correct in that part, but for the most part they are all itemized.

(Testimony of S. A. McAllister.)

Mr. Dougherty: They do not have January 1, 1947, balances there? A. No.

Mr. Dougherty: Or 1948?

A. I think not. I just got ahold of this book yesterday. I haven't had a chance to look at it. I would say it just goes up to 1946, the end of December, 1946. I haven't seen any '47 or '48 entries here (looking through ledger).

Mr. Dougherty: So, as I understand it, you haven't made an examination of this?

A. Well, my experience as an accountant teaches me that apparently it is in balance. I could strike off a balance sheet, if that is what you want.

Mr. Dougherty: Could you, as of the end of '44?

A. I think so.

Mr. Dougherty: I thought your testimony was that some of the '44 sheets were gone?

A. Some of these items do show balances as of January, '46, but it wouldn't have any relation to '44.

Mr. Dougherty: But are all of the '44 sheets there? [67] A. I think they are, -yes.

Mr. Dougherty: What balance does it show for the asset balance for trucks and trailers?

A. Account No. 1222 shows a total asset value of \$63,949.49, and on Account No. 2521, termed as "Reserve for Depreciation — Trucks" it shows a credit indicating a reserve set up of \$47,432.59.

Mr. Dougherty: As of what date is this, Mr. McAllister?

(Testimony of S. A. McAllister.)

A. Well, this is as of December 31, 1946.

Mr. Dougherty: What is the figure as of December 31, 1944?

A. Well, it shows an asset value of \$68,238.96 but that part of the "Reserved for Depreciation" sheet is not complete. It has a balance as of January 1, 1946, hence I would have to take the trial balances for '44 and '45 to figure out the depreciation to get the reserve set up.

Mr. Dougherty: So, then, some of the '44 sheets, or at least one of them, seems to be missing?

A. Yes, but the balance sheet is there. It can be worked out. If you want a trial balance as of December 31, 1944, I am sure it can be worked out with the books we have.

Mr. Dougherty: How long have you had possession of this volume?

A. I just got it yesterday.

The Referee: Where has it been?

A. Over at the Rand Truck warehouse.

The Referee: Well, had you had it before? [68]

A. I had some of the books, your Honor, but these old books I didn't take. I took the current books; that is, for about a year back.

Mr. Dougherty: Your Honor, I don't want to impede the progress of this. If someone who has knowledge can assure me that this is the volume I have no particular objection to its being received.

The Referee: Mr. McAllister, did you remove that sheet from this volume, this Exhibit 28?

(Testimony of S. A. McAllister.)

A. Yes, sir, I did.

The Referee: Could you reinsert it, please?

A. Yes (reinserting sheet previously marked Trustee's Exhibit 28 for identification).

Mr. Miller: Mark the ledger on the outside cover.

(Thereupon a green-backed ledger was marked for identification as Trustee's Exhibit No. 28.)

The Referee: Do you want Mr. Taylor to identify this book?

Mr. Miller: Maybe he could identify it but he didn't make the entries.

The Referee: I am aware of that, but I wanted to know if he was in charge of this. If you are going to put him on I will reserve my ruling.

Mr. Miller: We have no further questions of Mr. McAllister. We have one other witness.

Mr. Dougherty: No inquiries. [69]

### BERYL B. TAYLOR

was thereupon produced as a witness in behalf of the Trustee and, being first duly sworn, was examined and testified as follows:

#### Direct Examination

By Mr. Bollenback:

Q. Mr. Taylor, you were formerly connected with the Rand Truck Line?

A. I was, yes, sir.

(Testimony of Beryl B. Taylor.)

Q. In what capacity?

A. At the time of filing bankruptcy I was president.

Q. And how long had you been connected with the company prior to that time?

A. Since August 15, 1946.

Q. You have an exhibit in front of you, Trustee's Exhibit 28 for identification, which purports to be a ledger. Will you examine it and tell me whether you can identify that as a part of the books and records of the Rand Truck Line?

A. I am sure it is. I recognize all the handwriting. I had nothing to do with making the entries myself.

Q. Will you say it a little louder, Mr. Taylor, please?

A. I said I am sure it is because I recognize all the handwriting but I didn't prepare the book myself.

Q. You didn't prepare the book yourself. Was it made in the course of the ordinary business of the Rand Truck Line?

A. It was made by a party who was, prior to 1946, in the employ of [70] the Rand Truck Line for the purposes of preparing their financial statements and making their general ledger entries.

Mr. Bollenback: At this time we reoffer it.

Mr. Dougherty: No objection, your Honor.

The Referee: It may be received.



(Testimony of Beryl B. Taylor.)

(Thereupon, the ledger heretofore marked as Trustee's Exhibit No. 28 for identification was marked as received in evidence.)

Mr. Bollenback: Will you mark this?

(Thereupon a sheet headed "Analysis of Account No. 1650 'Other Investments—Officers' " was marked for identification as Trustee's Exhibit No. 29.)

Q. Mr. Taylor, I am going to hand you Trustee's Exhibit 29 for identification, which purports to be an Analysis of Account 1650, Other Investments—Officers, and ask you whether or not you took that information off of the books and records of the Rand Truck Line?

A. It was taken from the records, yes.

Q. By you or by someone under your direction?

A. Yes.

Mr. Bollenback: Now, your Honor, I don't know whether that is particularly relevant or not. It does show that some payments that were made to Otto Heider were charged to the account of the officers of the Rand Truck Line. It is offered in evidence in order that this Court might have all the evidence in front of it, [71] and if there is going to be any strenuous objection to it we will withdraw our offer.

Mr. Dougherty: No objection, your Honor.

The Referee: It may be received.

(Thereupon, the document heretofore marked for identification Trustee's Exhibit No. 29, was marked as received in evidence.)

(Testimony of Beryl B. Taylor.)

The Referee: From what source was that taken, may I ask?

A. Well, the 1659 account is a general ledger account and it could be traced back to the original book of entry to determine what they were and to whom they were paid.

Mr. Bollenback: At this time, your Honor, in order to avoid any oversight, the Trustee desires to reoffer in evidence Trustee's Exhibits 1 to 29, inclusive.

The Referee: Some of those were marked in the previous hearing, is that right?

Mr. Bollenback: They were, your Honor, and some of them have been marked twice, but the present set of numbers runs from 1 to 29. There are some duplications, but just in order that we don't overlook something, it is my desire to reoffer all of the exhibits that have been introduced.

The Referee: They will be received, subject to the objections which have been made in the record from time to time.

Mr. Bollenback: And now, your Honor, at this time the Trustee desires to amend his Third Objection to Proof of Claim, commencing [72] in the middle of page 4, and the reason for the amendment is that the evidence at this point does not disclose that any greater sum than \$31,500 was ever paid by Otto Heider to anybody on this mortgage, the first one, and in the first objections I did set out \$31,500 on line 2 of page 2, but in pleading the third defense the figure of \$36,500 was used be-

(Testimony of Beryl B. Taylor.)

cause that is the figure Mr. Heider stated on his deposition at the previous hearing.

The Trustee now desires to amend that to conform to the proof up to the present time of \$31,500, and that will necessarily change the other figures and the percentages in the objections to the claim. It will deduct \$5,000 from the principal and add \$5,000 to the interest, and then the claim balance of \$13,000 that was claimed to be due at the time it was refinanced would—a different proportion of it would be unpaid principal and unpaid interest, and it throws the computation completely off as to the second mortgage. However, the principle is there in essence, and that is that it was, in fact, an acrimonious transaction, and it is merely the details in how acrimonious it was for which this amendment is sought.

Mr. Dougherty: We object, your Honor. Of course, the amendment cannot be made as a matter of course. It can only be made by a legal court. Secondly, the objections as filed, are the sworn statement of the Trustee. I hesitate to be a party to any suggestion that the Trustee would care to deviate in any respect [73] from his sworn statements. Thirdly, we object again on the ground of laches. We have been unable to find any case where any court has allowed objections or amendments to objections to be filed at this late date. I am speaking of any reported case. Collier's Bankruptcy Manual indicates such tardy amendments cannot be

(Testimony of Beryl B. Taylor.)

filed either by the trustee or by anyone, and we would renew—we would object to the amendment on the same ground that we have objected to the objections being received.

The Referee: This amendment is in the nature of an amendment to the pleadings to conform to the testimony, is it not?

Mr. Bollenback: That is our position, your Honor, and further, Mr. McAllister is not in the position of the ordinary litigant who swears to a pleading. He has necessarily filed these pleadings as a result of hearsay. He didn't have any personal knowledge of the transaction so he should not be bound by any claimed admission.

Mr. Dougherty: If the Court please, I have always conceded the function of a trustee to make a preliminary examination. In this instance 7 years, approximately, have been allowed for that. While in minor matters we would have no objection to an amendment to conform with what counsel's idea of the proof is—in fact, however, the proof here has shown a far greater sum than alleged. However, as I understand this pleading, it was the informed judgment of the Trustee that that was the correct figure, and I have heard nothing which would in any way impair that judgment, [74] and it is a sworn statement.

The Referee: I am inclined to allow the amendment. It seems to me under the Rules of Civil Procedure they are very liberal in allowing amend-

(Testimony of Beryl B. Taylor.)

ments to pleadings, and this is in the nature of a pleading, being an objection to a claim.

Mr. Dougherty: Well, the Court has ruled. I was going to comment that I had never known of an amendment being allowed during trial in a Federal Court, but——

The Referee: I may say now that I didn't rule on the Supplemental Objections to the claim of Otto Heider. I don't see that they said anything, one way or the other. Therefore, I will sustain counsel's objection to this Supplemental Objection to Claim.

Mr. Bollenback: The Trustee has nothing further.

Mr. Dougherty: You may step down, Mr. Taylor.

(Witness excused.)

Mr. Dougherty: The Claimant will call Mr. Heider. [75]

### OTTO W. HEIDER

was thereupon produced as a witness in his own behalf and, being first duly sworn, was examined and testified as follows:

#### Direct Examination

By Mr. Dougherty:

Q. Now, Mr. Heider, was your claim in this matter filed on or about June 23 of 1949?

A. That's right.

The Referee: Just for the record, it was filed

(Testimony of Otto W. Heider.)

June 30th. If you would like you may refer to the original claim.

Mr. Dougherty: Thank you.

Q. Were the Trustee's objections to your claim served on you on or about January 26 of 1956?

A. Yes, a copy of it.

Q. Yes.

A. That was the first I had knowledge that there were any objections to the claim.

Q. Do you recall the prior hearing on this matter? A. I do; about seven years ago.

Q. About July 6 of 1949?

A. That's right.

Q. Do you recall the statement of the Referee at that time that if the Trustee had any objections to the claim as filed, he would make those objections?

A. Yes, he did, and I took the matter up with Mr. Bollenback at [76] that time.

Q. And what occurred at that time?

A. Well, he asked me if I would give a discount if they paid it off immediately and I told him I would. That was before the hearing and after he had investigated the matter, and I told him I would give a discount of three or four per cent because they wanted to pay it off and get the equipment free, and I agreed to it.

Mr. Bollenback: Just a minute. I object to this statement that I made this offer after I had investigated it. He doesn't know whether I had investigated it. If he is going to testify to any conversa-

(Testimony of Otto W. Heider.)

tion with me let him say what I said and not his conclusions as to what I said. Further, it is not binding upon the Trustee.

The Referee: Well, you may continue to state what conversations you had with counsel for the Trustee. The objection as to what investigations he had made, I think, should be sustained.

A. (Continuing): Well, it was some time after the petition in bankruptcy had been filed that Mr. Bollenback contacted me.

Q. (By Mr. Dougherty): Mr. Heider, after 1949 and before 1946 have your office records been disrupted in any manner?

A. Yes, they have. The Bureau of Internal Revenue had them for two years and a half, all of them.

Mr. Bollenback: Just a minute here. I don't know just what the purpose of this thing is, for two reasons. There's been no [77] answer filed in this case. We don't know what he is trying to prove and what the disruption of his office records—Any disruption of his office records subsequent to the time of this original deposition is certainly immaterial because he produced his books and records at that time, and I would like to know the purpose. As I say, there is a complete absence of any answer, and actually it would probably be proper, technically, to move for a judgment on the ground that there hasn't been any answer, and he is attempting to plead laches, apparently. I am not sure, but if it is, it is an affirmative defense and we don't have any answer. I mean as far as the pleadings go, the

(Testimony of Otto W. Heider.)

objections are admitted because they aren't denied.

Mr. Dougherty: If the Court please, it is my understanding that it would be most improper for us to file any responsive pleading to the objections. First, it is my understanding that under the Federal Rules replies are not allowed unless a reply is directed by the Court. There has been no reply directed in this instance. It is my understanding that the claim is in the nature of a complaint and the objection is in the nature of an answer and this is the form for the court proceedings, and it is so stated in Collier.

With reference to what this line of testimony seeks to develop, counsel is quite correct. We are attempting to show laches.

The Referee: I think you made that objection previously. [78]

You may proceed with your testimony, and, of course, subject to cross-examination.

Q. (By Mr. Dougherty): Mr. Heider, did the Bureau of Internal Revenue return all of your records to you?

A. No; they didn't return all of them. They had all of them and they didn't return all of them and they still have some of them.

Q. Can you now present documentary and other proof which you could have presented—that is, to refute these objections, which you could have presented, say in 1949?

A. I think that I could have gotten some more books and records if they hadn't all been worked



(Testimony of Otto W. Heider.)

over for two and a half years by somebody other than myself.

Q. I believe, Mr. Heider, you stated that it was your understanding that objections would not be filed?      A. That's right.

Q. What gave you that impression?

A. Well, after Mr. McAllister was appointed Trustee, Mr. Bollenback contacted me to pay it off, so I just dropped the matter and thought that was the end of it and never did any more work on it.

Q. Did the fact that no objections were filed for many years tend to change your impression at all?

A. No complaint of any kind has ever been made to the claim until this year.

Q. Now, Mr. Heider, do you, of your own personal knowledge, know [79] anything about the assets and liabilities of the Rand Truck Line for any of the periods herein involved?

A. Well, generally; not in detail.

Q. What was your understanding of its condition, say in 1944?

A. Well, my understanding was that they were in very good and substantial position—an operating, going concern, getting their assets in promptly and paying current bills promptly.

Q. Did they obtain equipment financing from you from time to time?

A. Considerable, on different items that they needed in their rolling stock, more than anything else. I did, from time to time, finance trailers or

(Testimony of Otto W. Heider.)

trucks or whatever pieces of equipment they wanted.

Q. Generally, how did they keep up their accounts with you?      A. Very good; very good.

Q. Do you know what their financial reputation was in the community or communities in which they did business?

Mr. Bollenback: Oh, I object.

A. Well, in my community, Sheridan and Willamina, where they did business, their reputation was excellent.

Q. And did that excellent reputation involve their paying their current liabilities promptly?

A. It did so far as I knew. I had no occasion to know otherwise.

Q. Did you at any time have any information that the Rand Truck Line might be insolvent?

A. No, I knew that they had the fire difficulty, and it was my [80] understanding, because of freight and things that they had in the warehouse, that they did suffer a very substantial loss, but outside of that fire difficulty, I didn't know of any difficulty whatever.

Q. As a matter of fact, Mr. Heider, if you had realized that there might be any insolvency there——

Mr. Bollenback: Oh, just a minute, your Honor. I am going to object to that question, at least.

Mr. Dougherty: Counsel might wait until he hears the question.

(Testimony of Otto W. Heider.)

Mr. Bollenback: I have heard enough of it that I know I am going to object to it.

The Referee: Let him finish.

Mr. Bollenback: Go ahead and complete it for the purpose of the record.

Q. (By Mr. Dougherty): Had you even suspected, Mr. Heider, that the Rand Truck Line was insolvent, would you have continued to loan it money?

Mr. Bollenback: I am going to object to that, your Honor, as being purely a hypothetical question——

A. No.

Mr. Bollenback (Continuing): ——and I ask the witness not to answer until I make my objection. I was stopped in making my objection. Until the objection has been completed I have the right to the same courtesy. I ask that the answer be stricken, your Honor. [81]

The Referee: I think it is going a little far afield. Mr. Heider was financing this company on what he thought to be a secured basis, anyway, so I sustain the objection.

Q. (By Mr. Dougherty): Mr. Heider, did you ever make any advances to this company without any immediate security?

A. No, I think that only a time or two I gave them checks—just what dates and amounts I can't recall, but I think I did without any security just as an accommodation.

Q. But only in a limited number of instances?

(Testimony of Otto W. Heider.)

A. Very limited; very limited.

Q. Did you purchase this mortgage executed by Rand Truck Line—did you purchase it from the payees named in that mortgage?

A. Yes, I purchased it from the payee named in the mortgage.

Q. And they assigned that mortgage to you?

A. Yes, assigned and transferred it to me, and I am the owner and holder of what you call the second mortgage, I guess—note and mortgage.

Mr. Dougherty: If the Court please, the assignment to Mr. Heider is Trustee's Exhibit No. 10, which was here all the time although we didn't know it. Now, this second mortgage, and also the first mortgage, was interest included in the principal amount?

A. In the balance amount due—the original balance the interest was included, that's right.

Q. Was the apparent interest collected in full?

A. No, because when I wrote the second mortgage, as I recall— [82] now, this is 7 years ago, and I haven't looked it up since, but I am just giving you my memory—there was a substantial amount of discount given on the first mortgage when I wrote the second mortgage—approximately \$900. I am not exactly sure of the amount, but there was a substantial amount of discount given.

Q. In other words, is it correct to say, Mr. Heider, that you gave them a receipt for moneys which you, in fact, did not receive?

A. Yes, because there were some payments yet

(Testimony of Otto W. Heider.)

to accrue on their first mortgage, and writing up the second mortgage they would be entitled to a refund on that unearned interest, so to speak.

Q. Referring to a group of papers marked Trustees' Exhibit No. 26, does that show an occasion where you gave him credit of \$960 in interest which was not, in fact, collected?

A. That is what I had in mind. I hadn't seen that for 7 years, but 960 was the amount. That's right. That is on what we would call the first mortgage.

The Referee: That is all that was unearned at the time you rewrote the mortgage in '46?

A. That's right; \$960 is unearned interest. It is marked here on the last payments of the mortgage.

Q. (By Mr. Dougherty): Were the installment payments on the mortgage delinquent at any time?

A. Oh, yes; they were delinquent at different times, which I wasn't concerned about particularly. They did get behind. [83]

Q. Did you charge any additional interest on the delinquent payments?

A. No, I didn't; I didn't charge them any additional interest on the delinquent payments.

Q. Is it correct to say, then, that there would have been additional interest due which wasn't collected?

Mr. Bollenback: I am going to object to that as being a conclusion unless he can show dates and times and amounts——

A. The note should provide——

(Testimony of Otto W. Heider.)

Mr. Bollenback: Just a minute. Unless he can produce the dates, the amount of interest, the time that it was past due, and how much interest was charged or would have accrued, to say that some other interest would have accrued is merely a conclusion.

The Referee: I think I am going to have to sustain that objection.

Mr. Dougherty: If the Court please, of course the reason that we cannot produce the records is because of the delay in making the objections.

The Referee: Isn't there a record of when these payments were made?

Mr. Dougherty: This appears to be a partial record, your Honor, and it does show that they were made at odd times—weren't made with particular regularity, and it does show that some payments were skipped, but I don't believe that it is a complete record. [84]

The Referee: Well, that record may be considered in connection with your question. Is that record an exhibit?

Mr. Dougherty: Yes, your Honor. They all have exhibit numbers.

The Referee: All right, that is fine.

Mr. Dougherty: Well, they all have exhibit numbers but this one page seems to have become detached.

The Referee: Keep them together, then.

Q. (By Mr. Dougherty): What was the amount of the obligation due and unpaid, Mr. Heider?

(Testimony of Otto W. Heider.)

A. At the time I filed the claim, twelve thousand-something. I have got a copy in my files here of the claim. You have the claim there. I know that the amount in the claim is correct—proof of claim.

Q. Was the proof of claim prepared from your books and records? A. At that time, it was.

Q. Were those books and records kept in the ordinary and regular course of your business?

A. They were.

Q. Were all of the entries made in those books and records made by you personally?

A. By me, personally and Miss Lawrence, who was working for me for thirty years.

Q. If they weren't made by you personally, were they made under your supervision? [85]

A. Yes, they were, in my office.

Q. And did the claim, as made, reflect those records? A. Just exactly as they were.

Mr. Dougherty: No further inquiries, your Honor.

### Cross-Examination

By Mr. Bollenback:

Q. Mr. Heider, are you a member of the Oregon State Bar? A. Yes.

Q. How long have you been practicing law in the State of Oregon?

A. Oh, I don't know, about forty years, pretty close.

Q. You were first admitted in what year, do you remember?

(Testimony of Otto W. Heider.)

A. '15, but I didn't practice there for part of the earlier years very much, that is, the first five years.

Q. Well, you have been a continuous member, then, for about 41 years, is that right?

A. Well, I will in August of this year.

Q. Now, you say that you didn't have any knowledge that the Trustee was going to object to this claim of yours until January, 1956, is that what I understood you to say?

A. Yes, Mr. McAllister—

Q. Just a minute. Answer me, "Yes" or "No." Is that what you say?

Mr. Dougherty: If the Court please—

Q. (By Mr. Bollenback): Now, you can explain if you want to, [86] but I want an answer first.

Mr. Dougherty: If the Court please, I will object to counsel arguing with the witness.

The Referee: You need not argue.

Q. (By Mr. Bollenback): January, 1956?

A. Yes, I received the objection January, '56.

Q. And that was the first you knew that the Trustee was going to object to this claim?

A. Well, I think that was the first objection ever served on me, except the Circuit Court procedure.

Q. There was a Circuit Court lawsuit against you, wasn't there? A. It is still pending.

Q. In which the Trustee is seeking to obtain 40,000 or more from you, is that right?

A. And some other defendants, too.

Q. And it grows out of this same transaction, doesn't it? A. Yes.



(Testimony of Otto W. Heider.)

Q. And did you think that the Trustee was going to sue you for \$40,000 and still not object to your claim for \$11,000? A. As a matter of fact——

Q. Just answer me, "Yes" or "No."

I would like to have the reporter read the question and the witness give a yes-or-no answer and then make any explanation he desires, but a yes-or-no answer first.

Mr. Dougherty: I must instruct you, Mr. Heider, that if [87] it is a question impossible to answer by "Yes" or "No," then you need not so answer it.

(The question was read.)

A. That answer has to be qualified.

Mr. Bollenback: Well, go ahead and answer.

A. Mr. McAllister and I have been taking this up with one another for a considerable time towards settlement and compromise and we talked it over at different times over the last seven years, and I never did think that the lawsuit in the Circuit Court was brought in good faith and with any intention of ever recovering on it. In fact, I was positive of that, that it was never procured with any intention of continuing in good faith against any of the defendants, but it was simply to cover up a claim that I had filed in this court. That was the only purpose of the lawsuit in the Circuit Court, and that has been ascertained by the case being thrown out of court several times since you filed it.

Mr. Bollenback: Well, now, just read the question again, and I ask the Court to have the witness

(Testimony of Otto W. Heider.)

answer the question "Yes" or "No." He has given his explanation; now I would like to have an answer.

(The question was reread as follows: "And did you think that the Trustee was going to sue you for \$40,000 and still not object to your claim for \$11,000?") [88]

A. Yes, I did.

Q. (By Mr. Bollenback): Now when did the Internal Revenue first show an interest in your books? A. In December, 1950.

Q. In December, 1950? A. Yes.

Q. Now this hearing was had in July of 1949, isn't that right? A. Yes.

Q. And you were asked by the Court to produce all your books and records concerning this transaction, weren't you? Answer me "Yes" or "No."

A. Well, not until after they had a hearing. We never had a subsequent hearing before that. I was asked to bring out records at a subsequent time.

Mr. Bollenback: Read the question again, please.  
(The last question was read.)

A. As far as it was possible to do so, yes.

Q. (By Mr. Bollenback): All right, so you did.

A. No, not all of them.

Q. In other words, you disobeyed the Court's instructions?

Mr. Dougherty: If the Court please, I must object to counsel misrepresenting the record. The Court instructed Mr. Heider to bring an itemized statement of receipts and disbursements and the

(Testimony of Otto W. Heider.)

Court did not request or instruct Mr. Heider to bring all of his books and records, and counsel well knows [89] what the record shows.

Mr. Bollenback: I shall read what the record shows, reading from Referee's statement on page 4 of the transcript, quoting from the Referee—referring back to page 3: "Now, at the time Mr. Heider sent up this proof of claim he wrote me a letter in which he asked whether it would be necessary for him to appear today in view of the fact that he had filed his proof of claim, and I wrote acknowledging receipt of the claim and of his letter. I said, 'The claim is deficient in that you did not include therein an itemized statement of monies disbursed or received by you in connection with any transactions or payments made in connection with said mortgage or the prior mortgage executed September 18, 1944.' In that I was following the language of the order. I said, 'Please bring such a statement with you at the hearing scheduled in my courtroom on Wednesday, July 6, 1949, at 10:00 o'clock a.m. Also bring with you your original records showing receipts and disbursements in connection with the two mortgages. The hearing set for next Wednesday is for the purpose of receiving proof of the balance due on your mortgage and of all transactions in connection with it so that the Court may determine the validity of the mortgage and the amount owing thereon.' "

Q. Now, did you, in response to that request of the Court, produce your original records?

(Testimony of Otto W. Heider.)

Mr. Dougherty: Now if the Court please— [90]

The Referee: I think you did, didn't you—those checks and everything?

A. Yes, as far as I could at that time.

The Referee: Well, how do you answer the question? He asked you whether you produced them or not.

A. Well, yes, so far as I could get them together at that time.

Q. (By Mr. Bollenback): And the interference of the Internal Revenue did not occur until after that time?

A. Well, not until after that hearing, no.

Q. Now did you ever loan any money to Bob Rand before the Markees took the Rand Truck Line over? A. Personal loans to him?

Q. Corporation loans.

A. I believe these loans we are talking about are the only loans—these two to the Rand Truck Line corporation were the only loans I ever made them.

Q. Well, I got the impression that you had made other loans and that they had established a credit with you. A. To Bob Rand?

Q. Yes.

A. Well, just on vehicles, just like I told you before, just for trucks or trailers or rolling stock.

Q. You had loaned money to Bob Rand for trucks and trailers?

A. Well, to the Rand Truck Line. Bob Rand was the principal [91] owner.

Q. Now you say you thought that they were

(Testimony of Otto W. Heider.)

solvent?      A. I knew they were solvent.

Q. You knew they were solvent?

A. Yes, I knew they were solvent.

Q. But you had some difficulty getting payments from them, didn't you?

A. No, I didn't have any particular difficulty. The only difficulty I had was once in awhile they would ask me to hold a check until they got in their monthly bills, sometimes. A check might be a few days overdue, so to speak, before they got in their collections, and I think I did hold up the check.

Q. In other words, they weren't very solvent if you had to hold their checks?

Mr. Dougherty: Object——

A. They had a very solvent record in my community.

Q. (By Mr. Bollenback): Did you ever examine the books of the corporation?

A. I am not a bookkeeper or auditor.

Q. Just answer the question.      A. No.

Q. You never did?

A. Oh, I have seen some of the books but I never made an examination of them.

Q. How did you know they were solvent then? [92]

A. Because I knew they paid their bills promptly.

Q. Did you know their assets exceeded their liabilities?

A. Well, these books show that their assets exceeded their liabilities.

(Testimony of Otto W. Heider.)

Q. At what time, Mr. Heider?

A. Well, in '44 and '45 and '46.

Q. Taking your mortgage into consideration?

A. Well, taking any of their liabilities into consideration, I would say.

Q. Do you realize that this first mortgage that you took did not appear on the corporation books for about two and a half years after it was executed?

A. I didn't keep the books of the company at any time.

Q. Did you notice in your examination of these books that that didn't show up on the corporation liabilities? A. I never checked that at all.

Q. Then you didn't know whether they were solvent or not, did you?

A. Well, I knew they met their obligation to me, is all.

Q. Now you mentioned that you had negotiated with Mr. McAllister to compromise this claim.

A. We discussed it several times. We never arrived at any figure, we never agreed on any amount.

Q. Did you ever make an offer?

A. And neither did he ever make an offer to me—I mean a [93] firm offer.

Q. Did you ever make an offer to him?

A. I don't think he ever asked me to make a definite offer.

The Referee: I don't think I should consider this.

Mr. Bollenback: It isn't proper, your Honor,

(Testimony of Otto W. Heider.)

but he brought it up. It isn't a proper part of the testimony but he raised the question.

Q. Mr. Heider, do you remember when you were served with the complaint and summons in the Circuit Court suit with relation to the taking of this deposition on July 6, 1949?

A. Oh, it was some time afterwards. I could guess.

Q. Do you have your file with you on that case?

A. When the first complaint was filed?

Q. Yes.

A. I think it was five or six years ago.

Q. Let's get the date that first complaint was filed or the date of your first appearance in the case.

A. I think it was in '47.

Mr. Dougherty: My file goes back to a complaint which was filed on September 3, 1952.

Mr. Heider: Oh, it was prior to that.

Mr. Dougherty: I don't have the first complaint.

Mr. Heider: Mr. Bollenback should have it. I think he prepared it.

Mr. Bollenback: My files of the Rand Truck Line are [94] voluminous and I didn't bring that one with me.

Mr. Heider: Maybe I can give you the date if you want it. I think there have been five amended complaints filed, and I think you are due now for another one. (Looking through file.) Here are some papers back in 1950, so I know it was six years ago.

Mr. Miller: Perhaps we can stipulate for the record that whatever the court record in Mult-

(Testimony of Otto W. Heider.)

nomah County shows is the original filing date. Is that right, Mr. Dougherty?

Mr. Dougherty: Yes. I am certainly not stipulating, though, that those first few amended complaints would put him on notice.

Mr. Miller: All I am asking is whether the commencement of a suit, whether you liked it or not, was made on a certain date.

Mr. Dougherty: Now please let's keep this on a professional basis.

The Referee: That will be understood.

Q. (By Mr. Bollenback): Did you turn any records involving this transaction over to the Bureau of Internal Revenue?

A. They had all of them, checked the figures completely.

Q. Concerning this transaction?

A. Exactly.

Q. They took your original records?

A. They did, my original books and records and checks. Any, of course, they couldn't get, I told them where the records [95] were on file down here. I don't know if they came here and checked them over.

Q. What papers did you turn over to them involving this transaction—what records did you turn over? A. These files right here, 1, 2, 3.

Q. And what else?

A. And my own bookkeeper's books—original records.

Q. Original records on this transaction?



(Testimony of Otto W. Heider.)

A. On this and other transactions.

Q. Did you get those books back?

A. I got some of them back.

Q. Did you get them back on this transaction?

A. I don't think I did.

Q. Do you remember at the time of the taking of this other deposition when you insisted that these yellow sheets were the only ones in your original transaction?

A. Well, I had these files here.

Q. Just answer my question.

A. They were records of payments, yes.

Q. They were your original records?

A. Yes, they were my original records, but some of the notations on those records were probably put on other books, but they were my original records that I had here before.

Q. And they were in the Bankruptcy Court?

A. I told them where they were. Whether they called on [96] Mr. Snedecor and got them, I don't know, but they knew where they were.

Q. Did you turn any cancelled checks over to them?

A. Not on this transaction in particular, but all of them. If there were any that weren't here they had them.

Q. Did you turn any other cancelled checks over to them that involved this transaction?

A. I don't know that I turned any others because I think most of the checks have been introduced here.

(Testimony of Otto W. Heider.)

Mr. Bollenback: That is all.

The Referee: Do you have any further questions?

Mr. Dougherty: Yes, if the Court please.

### Redirect Examination

By Mr. Dougherty:

Q. Isn't it a fact, Mr. Heider, that none of the first two or three complaints——

Mr. Bollenback: Now, if the Court please——

The Referee: Go ahead.

Q. (By Mr. Dougherty): Isn't it a fact, Mr. Heider, that none of the first two or three complaints filed by the Trustee raised any of the issues raised by these objections here?

A. Well, that is my understanding.

Mr. Bollenback: Just a minute. Just a minute. I am going to object to that as calling for a conclusion of law.

Mr. Dougherty: You have qualified the witness as a lawyer [97] with 41 years' experience.

Mr. Bollenback: Produce your evidence, then. Put your pleadings in evidence if you want to, but let's not have conclusions of law.

Mr. Dougherty: I am asking Mr. Heider as a matter of fact——

Mr. Bollenback: I am objecting to the question. Put the pleadings in evidence. That is the best evidence.

The Referee: I will let him answer it, I think,

(Testimony of Otto W. Heider.)

and you may submit your pleadings into evidence if you like.

A. That is my recollection of the matter, that these objections weren't raised in those first complaints, and I haven't checked them for a long time but that is my recollection of it.

Q. (By Mr. Dougherty): Let's take the one matter of usury. Isn't it a fact that Mr. Bollenback didn't introduce that into this litigation until just a couple of years ago?

A. That's right, that's correct.

Q. And that is only one example.

Mr. Bollenback: I suggest that Mr. Dougherty be sworn.

Mr. Dougherty: If the Court please, I should like to go back now and do something which I should have done on direct examination.

The Referee: You may proceed.

Mr. Dougherty: I will ask the reporter to mark these six pieces of paper.

(Thereupon, two original checks and three carbon copies of checks purporting to have been executed by Otto W. Heider to Rand Truck Line or to Rand Truck Line and others, in the year 1946, and a note executed by Floyd L. Long, dated May 15, 1944, was marked Claimant's Exhibit No. 30 for identification.)

Q. (By Mr. Dougherty): Mr. Heider, I show you 6 documents marked Claimant's Exhibit No. 30

(Testimony of Otto W. Heider.)

for identification, and ask you if you will tell us what those are.

A. Those are payments to the Rand Truck Line corporation in '46 and these carbon checks are exact duplicates of the original checks, and this note here, Floyd L. Long, dated May 15, 1944, was one of the obligations that was written into what we call the, as I recall—into the mortgages that are involved, and these two checks were on other transactions but were eventually incorporated into what we call the last mortgage.

Q. May the originals of some of these carbon copies be in evidence already?

A. I think they are. The originals of the carbon copies, I think are already in evidence.

Mr. Dougherty: We offer Claimant's Exhibit No. 30, your Honor.

Mr. Bollenback: I would like to see it, please.

I would like to ask the witness a preliminary question, your Honor. [99]

Why did you hold these checks back without introducing them before?

A. Couldn't find them.

Mr. Bollenback: I mean today.

A. I had them here all day long.

Mr. Bollenback: Why did you claim that the Bureau of Internal Revenue had your cancelled checks and you couldn't produce any more evidence?

Mr. Dougherty: The witness made no such claim.

(Testimony of Otto W. Heider.)

Mr. Bollenback: Well, then his attorney did.

Mr. Dougherty: That is false likewise.

A. I didn't have all my records. I had about nine-tenths of them.

Mr. Bollenback: Now, if your Honor please, this is all under one exhibit and I don't know what I am going to do about all these checks. For the record we will object to any of this evidence going in on the ground it should have been introduced on the examination in chief rather than on redirect. It just appears that this witness was holding these documents back with the idea of not using them until he found it was necessary to use them, and then he produces some checks.

Now just a minute. I am not through.

And on the further ground that he has, by his own statement made not 15 minutes ago, said that he was unable to produce any further books and records because the Bureau of [100] Internal Revenue had taken his cancelled checks and had not returned them to him, and furthermore as to one of these documents—it is a note to Page & Page and made by a man by the name of Floyd Long, and neither Rand Truck Line nor Otto Heider shows up on the document, and what it has to do with this case is something I don't know, but I think that the bad faith of this man producing these checks at this late date, in view of his previous claims, is enough to discredit the entire transaction.

(Testimony of Otto W. Heider.)

Mr. Dougherty: If the Court please, first as to why they were not introduced before, they were before me and were covered up in a mass of papers. It is my oversight. Secondly, as to the statements of the witness, they have been merely that he is not now able to produce as much evidence as he would have been able to seven years ago. He has not made any claim that he wasn't able to produce any evidence now. Thirdly, with respect to the note to Page & Page, signed by Long, the witness' testimony was that that was some evidence of an equipment transaction which was included in his transaction with Rand Truck Line, and I should like, if there is any question about that, to examine the witness further with regard to that.

The Referee: Supposing you do that.

Mr. Bollenback: I suggest they separate the exhibit, your Honor, and mark that separately from the rest of them, but we also would like a ruling from the Court on our first objection, [101] that it should have gone in on direct examination.

The Referee: I am not going to take technical advantage of counsel and say that it cannot be introduced. The Court is quite liberal in allowing testimony to go in. I would allow the same to you. I do suggest that you make the checks one exhibit and help the Court by telling us what the purpose of them is, because I happened to be reading the record at the time you introduced them.

Mr. Dougherty: Yes. Then the five checks are

(Testimony of Otto W. Heider.)

marker Claimant's Exhibit 30. We have removed the note from the Claimant's Exhibit 30. They are checks from Otto Heider to Rand Truck Line, or copies of checks—that is, carbon copies of checks from Otto Heider to Rand Truck Line for various sums of money, all dated in 1946, and it was the witness' testimony that these represent advances made by Otto Heider to Rand Truck Line, which advances are reflected in the mortgages under consideration.

The Referee: Those were to enable them to purchase some equipment?

A. Yes, it was, and then when we made the second mortgage this was all picked up in the second mortgage—these checks were, and that note, too, of Mr. Long likewise represented equipment which was sold to the Rand Truck Line and I paid it off.

The Referee: All right. [102]

Q. (By Mr. Dougherty): Taking the check of March 19, 1946, for \$2,500, payable to Rand Truck Line, was that money advanced to them in connection with their purchase of a new Fruehauf van?

A. Yes, 24-foot, all-steel—a new van—4-wheel van.

Q. Well, tell us about any of the conditions.

A. This was for the purchase of a used '41 van.

The Referee: What is the amount of that check?

Mr. Dougherty: That is \$2,500.

Mr. Bollenback: Clear it up in my mind, Mr. Heider. Are these transactions in addition to the two mortgages, or what?

(Testimony of Otto W. Heider.)

A. No, they were incorporated in the mortgage.

Mr. Bollenback: In what mortgage?

A. In the last mortgage.

Mr. Bollenback: Oh. Both of them?

A. This one was incorporated in the first mortgage (indicating), but these were incorporated in the last mortgage.

Mr. Miller: Will you identify them for the record?

Mr. Dougherty: The one which has not been offered yet is the note.

The Referee: Well, as I understand it, after you had the first mortgage you assisted them in the financing of some additional equipment and had either conditional sales contracts or chattel mortgages on the equipment, and then you consolidated those when you took the second mortgage, with the original indebtedness which was given by the company to the stockholders [103] for the purchase of the stock.

A. Between the two mortgages, if you want to call it that way, I financed additional equipment.

The Referee: Yes, that's right. The Court understands it. The checks may be received in evidence.

(Thereupon, the five checks heretofore marked Claimant's Exhibit No. 30 were marked as received in evidence.)

Mr. Bollenback: I haven't examined them.



(Testimony of Otto W. Heider.)

The Referee: You may cross-examine later.

Mr. Dougherty: Will you mark this, please?

(Thereupon, a document purporting to be a promissory note executed by Floyd L. Long in favor of Page & Page Trailer Company on May 15, 1944, in the amount of \$3,786.00, was marked for identification as Claimant's Exhibit No. 31.)

Q. (By Mr. Dougherty): I hand you a note dated May 15, 1944, marked Claimant's Exhibit No. 31, and ask you if you can tell us what that is.

A. Well, that was made by Mr. Long to Page & Page Trailer Company, that manufactures here in Portland a Page trailer, and Mr. Long could not pay out on this note and the trailer was taken over by Rand Truck Line and this was incorporated into their mortgage, as Floyd L. Long lived at Grand Ronde and became insolvent and I did take the equipment back when I sold [104] it to Rand Truck Line, and then when they made the first mortgage they picked this up.

Q. So this is just some evidence of one of the items that went into the first mortgage?

A. Yes, that's right, and Mr. Long still lives at Grand Ronde, Oregon, the man that signed the note.

Mr. Bollenback: I never heard of the transaction before. I am going to object to it.

The Referee: What is the amount of it?

Mr. Bollenback: \$3,786.00, and it doesn't say how much—unless this witness is contending that he

(Testimony of Otto W. Heider.)

paid for the benefit of Rand, this entire amount, it is still incompetent and irrelevant. It doesn't prove anything. A. I didn't claim that.

Mr. Bollenback: Well, I am going to object to it until the transaction is aired.

A. I can explain it.

The Referee: Well, do you want the Court to understand that the mortgage given——

A. By Long.

The Referee: No, not that—the mortgage given to Mrs. Rand and assigned to you includes this indebtedness? It is the first time I have ever heard of it.

A. It is the first mortgage, not the second mortgage.

The Referee: The first mortgage is the one we are talking [105] about.

A. Yes, this indebtedness was included in the first mortgage, not the second mortgage.

The Referee: Who owed that indebtedness?

A. Well, I haven't got the mortgage any more. I forget how it was executed. Rand Truck Line owed the indebtedness.

The Referee: It was made payable to Mrs. Rand?

A. Well, made payable to Mrs. Rand and then assigned to me.

The Referee: Yes, but did the company owe Mrs. Rand some money?

A. I have forgotten the first mortgage. May I see the first mortgage a minute? I think I can clear

(Testimony of Otto W. Heider.)

that up if I can see the first mortgage. I think it is here. I returned the first mortgage to the Rand Truck Line when it was paid off by the renewal, and it is the one that is dated—I don't have that mortgage any more.

The Referee: Well, there is a copy of the mortgage there. Now, that mortgage was given to Mrs. Rand for the purpose of financing the purchase of the stock. How would that have anything to do with the note on some repossessed equipment?

A. It covered additional obligations besides what I did advance to the Rands. Mr. Rand testified that I paid him \$32,000, but it included an additional amount beside the \$32,000, and it was written into this mortgage. I consolidated it all into this mortgage because Mrs. Rand was not obligated on [106] this mortgage to pay it at all, and I consolidated some other indebtedness into this mortgage.

The Referee: No, you didn't in the first, did you? Did you in the first? You did in the second.

A. Yes, I did in the first as well as the second mortgage.

The Referee: And what are the items made up in the first mortgage, then? What are the items made up in Mrs. Rand's mortgage that you put in there?

A. Well, \$32,000, the checks, and some cash which Mr. Rand had in addition to the checks, and then not all of this note was in there but there had been some payments on it. I can ascertain, I think.

The Referee: I am going to sustain the objection

(Testimony of Otto W. Heider.)

on that offer, unless you can give me some more specific information from your records as to that.

A. I think I can get the information from my office.

The Referee: We may have oral argument. I can't accept that note as being any evidence with the vague statement of the witness. If you can get something specific for me you may do so, Mr. Dougherty, but it is too vague for me to understand.

Mr. Dougherty: It is my understanding, your Honor, that in this financing it was contemplated that Mr. Heider was going to loan the money to Rand Truck Line. Rand Truck Line already owed him some money.

The Referee: Well, then, I would like to have that [107] evidence. I will give you an opportunity to produce it if there is any evidence that at that time they owed Mr. Heider any money and it was incorporated in this obligation. I think it would be quite important to know that.

Mr. Dougherty: Well, we will do so with all of the evidence that we can on that point. Whether or not we can produce any, I don't know, your Honor. I suggest that 7 years ago such evidence could have been offered.

The Referee: I don't recall it ever being in any other testimony before.

Mr. Bollenback: May I ask the witness some questions, your Honor?

The Referee: Yes.

(Testimony of Otto W. Heider.)

Mr. Bollenback: Mr. Heider, at the time of the first hearing did you or did you not produce \$36,500 worth of checks and say that was what you gave for that first mortgage?

A. I think there were that many checks produced at that time.

Mr. Bollenback: Yes, and you said that was what you gave for the mortgage, isn't that right?

A. Well, this was also——

Mr. Bollenback: Just answer me. Isn't that what you said you gave for that mortgage at that time?

A. That amount in checks, I think.

Mr. Bollenback: And that the balance was with interest at 10 per cent, compounded [108] semiannually?

A. I might find the note and mortgage here. I will try.

Mr. Bollenback: I have another issue I would like to raise, your Honor, on this point.

Are you looking for something in particular, Mr. Heider?

A. Well, no. I can answer your question.

Mr. Bollenback: All right. I want to call your attention to the Earl Walden mortgage. So you won't be misled, I want to hand you Trustee's Exhibit 4, the Earl Walden mortgage. Now, that was a mortgage for \$1,080, payable in one year, is that right?

A. Yes.

Mr. Bollenback: And that included prepaid interest, did it not?

A. That's right.

(Testimony of Otto W. Heider.)

Mr. Bollenback: At what rate was the interest included?

A. I think the same as the others, 10 per cent.

Mr. Bollenback: Compounded semiannually?

A. Yes, I think it was.

Mr. Bollenback: Now, I want to hand you a check of a thousand dollars that you have just introduced in evidence, payable to Rand Truck Line or Earl Walden, and ask you if that is the check which you advanced in return for that mortgage.

A. Yes, there was another item there, though, that went into that besides this check. [109]

Mr. Bollenback: What was that?

A. I think there were some attorney's fees for services. I think I explained that to you originally.

Mr. Bollenback: Did you keep a ledger account of the services that you rendered to the Rand Truck Line?

A. Oh, I rendered services for them from time to time.

Mr. Bollenback: Answer my question.

Will the reporter read the question?

(The last question was read.)

A. I don't remember whether I kept one or not. I may have.

Mr. Dougherty: Are you through, Mr. Bollenback?

Mr. Bollenback: Beg pardon?

Mr. Dougherty: Are you through on that?

(Testimony of Otto W. Heider.)

Mr. Bollenback: No, I am not. I wanted him to answer that last question.

The Referee: He did answer.

Mr. Bollenback: What was it?

(The last answer was read.)

Mr. Bollenback: What services would you be rendering them in that connection, Mr. Heider?

A. Oh, matters we would take up with the Public Utilities sometimes, and routes, and things—just various matters when they would drop in there and ask for advice.

Mr. Bollenback: And how much was the fee that you charged that went into this transaction? [110]

Mr. Dougherty: Now, just a moment. He hasn't testified that he charged any fee. He said that that might be an explanation.

Mr. Bollenback: Well, what is the explanation, then, that you want to accept or admit?

Mr. Dougherty: Well, I want the explanation which was on the instrument itself, that this is the part over deductions, plus cash at various times.

Mr. Bollenback: All right, explain that, Mr. Heider.

A. (Reading): "Part over deductions plus cash, various."

Mr. Bollenback: Explain that.

A. Explain it?

Mr. Bollenback: Yes.

A. Well, it says here, "Part over deductions." I just told you it was probably for services.

(Testimony of Otto W. Heider.)

Mr. Bollenback: All right. What deductions?

A. For services rendered.

Mr. Bollenback: How much?

A. Well, probably \$30 or \$40.

Mr. Bollenback: For what?

A. Oh, for various and sundry matters.

Mr. Bollenback: For instance?

A. Oh, in regard to routes and one thing and another.

Mr. Bollenback: What did that involve?

A. What route did this involve? [111]

Mr. Bollenback: Yes.

A. I can't tell you now.

Mr. Bollenback: Yes, that \$35 item.

A. I can't tell you what route the matter involved—just things that might come up from time to time that they might ask about.

Mr. Bollenback: Did you ever bill them for it?

A. They paid it right there.

Mr. Bollenback: Did you ever send them a bill for services rendered?

A. No, they were in my office every week or two.

Mr. Bollenback: They were in there on your business, weren't they, Mr. Heider?

A. They were there on their business, too.

Mr. Bollenback: Did you ever appear before the Public Utilities Commission on behalf of the Rand Truck Line?

A. I had some correspondence with them.

Mr. Bollenback: Did you ever appear before the



(Testimony of Otto W. Heider.)

Public Utilities Commission in behalf of the Rand Truck Line?

A. I don't think I ever appeared before them.

Mr. Bollenback: Are you licensed to practice before the Public Utilities Commission?

A. I think I don't have to be admitted to write them letters.

Mr. Bollenback: Answer the question, please.

A. I have no special admission certificate that I know of. [112]

Mr. Bollenback: And you have never, as I take it, appeared before the P.U.C.?

A. Oh, yes, I have.

Mr. Bollenback: All right, when and where did you appear before them in relation to the Rand Truck Line?

A. No, I never attended a hearing for the Rand Truck Line, but I have on other matters.

Mr. Bollenback: Is it still your position that some of your checks are missing involving these Rand Truck Line matters?

A. I didn't claim that there were any missing, did I?

Mr. Bollenback: It is my understanding that you are claiming that the——

Mr. Dougherty: If the Court please, counsel has consistently misstated the record. I consider it a most unprofessional thing to do. What Mr. Heider has said——

(Mr. Bollenback laughed.)

(Testimony of Otto W. Heider.)

Mr. Dougherty: —and if counsel approves of his unprofessional conduct that is his choice—what Mr. Heider has said is that he cannot now produce as much evidence as he could have, had not Mr. Bollenback been guilty of laches in this matter.

Mr. Bollenback: All right, Mr. Heider, what evidence can't you produce now that you could have before?

Mr. Dougherty: How can he know? He knows that his files are missing.

The Referee: I think I have heard enough on this matter [113] of laches.

Mr. Heider: If the Court will give me an opportunity on what the Court asked about this mortgage on this loan, if they will consent to it, I think I can go through old files at Sheridan and send it to the Court.

The Referee: I think when we have finished this we will ask for briefs on certain matters of law and probably oral argument. At that time if you have some additional evidence you want to produce you may do so.

Mr. Dougherty: Should we withdraw that at this time, your Honor?

The Referee: Yes.

Mr. Bollenback: Withdraw what?

The Referee: That note.

Mr. Bollenback: Well, you haven't got it. It isn't in—the Long note.

Mr. Dougherty: It is in that group of papers, Mr. Bollenback.

(Testimony of Otto W. Heider.)

Mr. Bollenback: All right, you find it.

Mr. Dougherty: Why all these petty objections? That is what I was prepared to do.

Mr. Heider: I can either find the mortgage or get a certified copy of it, the mortgage that goes with that transaction.

Mr. Dougherty: I suggest counsel withdraw his notes from the exhibits. [114]

Mr. Bollenback: All right.

The Referee: Does anyone have anything further?

Mr. Heider: Here it is (producing the note).

Mr. Bollenback: Seriously, I have some more questions to ask this witness. Do you have anything you want to take up, Mr. Dougherty?

Mr. Dougherty: No.

### Recross-Examination

By Mr. Bollenback:

Q. Now, Mr. Heider, you have now made a statement that this original mortgage included some obligations of the Rand Truck Line in addition to the money that you advanced to the Rands or paid to the Rands. A. That is my understanding.

Q. Then when this mortgage was drawn, or before it was drawn, you knew you were going to take it over, didn't you?

A. I had no sure proof of it. I do buy mortgages; I don't any more, but I did then.

Q. Well, if you didn't know it was going to be

(Testimony of Otto W. Heider.)

taken over by you why did you include in it some other obligation that the Rand Truck Line owed you? A. You say why did I include it?

Q. Yes.

A. Because they were consolidating their debts as far as they could at that time. [115]

Q. Well, then you knew that you were going to take it?

A. Oh, I very likely understood I would buy it. I didn't buy it at the time it was drawn, but it was very likely understood because it was drawn in my office, so that is very likely proof I would take it.

Q. And included in there is an obligation you say the Rands owed at another time?

A. On some equipment.

Q. And as a part of this whole transaction there was an endorsement by Mrs. Rand without recourse, is that right? A. Yes.

Q. You never intended to look to the Rands?

A. I never intended to look to the Rands personally, let's say; no, I didn't.

Q. Now, Mr. Heider, what are the allegations that are contained in that first complaint filed over in the courthouse?

A. Well, I have been looking for it, Mr. Bollenback.

Q. Well, you testified that there isn't anything in there that was of any consequence. Just tell us what was in there.

Mr. Dougherty: If the Court please, to shorten this we will get photostats of the pleadings.

(Testimony of Otto W. Heider.)

The Referee: Yes, we will have those introduced.

Mr. Miller: Counsel was able to state as an expert a conclusion as to what was in there. We would like to have him.

The Referee: I would rather have them made a part and I [116] can tell.

Mr. Bollenback: I would like to ask this witness another question as an expert, your Honor.

Q. Isn't it a fact, Mr. Heider, that usury is not an affirmative matter but is a defense?

A. There is no usury involved in this case.

Mr. Dougherty: As a conclusion of law Mr. Bollenback's statement is false and has been ruled to be inaccurate by the Circuit Court of the State of Oregon.

Mr. Miller: We asked for the expert opinion of the witness, not his counsel.

Mr. Dougherty: I cannot stand back and allow Mr. Bollenback to try to confuse Mr. Heider on a matter of law which Mr. Bollenback has already lost in the Circuit Court.

Mr. Bollenback: I am glad there is a higher court.

Q. Mr. Heider, do you have a copy of your claim there? A. The first complaint?

Q. Do you have a copy of your claim there?

A. It is right here.

Q. A copy of your claim? A. That I filed?

Q. Yes, do you have that there?

The Referee: The original claim is there. I handed it to Mr. Dougherty awhile ago.

(Testimony of Otto W. Heider.)

A. I will identify the claim if you think it isn't properly [117] identified.

Q. (By Mr. Bollenback: Here it is, Mr. Heider. Why did you insert in this claim the statement, "Affiant further states said debt herein proven and this claim are free from usury, as defined in the laws of the State of Oregon wherein the debt was contracted"? A. Free from usury?

Q. Yes, because it is a fact you knew at the time the claim was filed, at that time in June, 1949, that usury was being claimed in this, didn't you?

A. In the first complaint? I was just looking for a copy of the first complaint and I don't recall that you mentioned usury.

Q. In June, 1949, you filed a claim with the Bankruptcy Court in which you make the statement that the claim is free from usury.

A. I copied that out of a form book now, and that was part of the form.

The Referee: Let me have that claim.

A. I think that was copied out of a form book.

Q. (By Mr. Bollenback): You did say in your statement previously that you had computed interest at 10 per cent compounded semiannually, didn't you? A. Yes, I did.

Mr. Dougherty: Mr. Heider, you didn't say that that is the way the interest actually paid would work out. [118]

A. No.

Mr. Dougherty: Because in fact, some of the interest that was computed wasn't, in fact, paid.

(Testimony of Otto W. Heider.)

Mr. Miller: Your Honor, he is his client and he is an attorney and he is leading him right down the way.

The Referee: Well, most of this seems to be argument between counsel instead of testimony. You can make your arguments later. Is there anything else?

Mr. Bollenback: I hope to submit a memorandum of authority, your Honor, not with the idea that it is exclusive. I might want to put in some more, but fundamentally and basically it sets out the Trustee's position. I don't think that there is any need or reason to go into a long extended argument at this time. I do feel that a summary of the facts in this case is going to be quite important and I would ask the Court to give me permission to take the deposition of Mr. Heider out of the office here and prepare a summary of fact from that and the exhibits—I can get the exhibits here—with transcript references, and I will serve a copy on counsel.

The Referee: Well, I suggest that you supplement your brief by a summary of the facts which you claim are now in evidence and then that will give counsel for Mr. Heider an opportunity to summarize the facts as he sees them or to object to any facts that you state are a part of the record, and also answer your memorandum. Is that satisfactory, Mr. Dougherty? [119]

Mr. Dougherty: Thank you, your Honor.

The Referee: Now, there are one or two things left open. The question of the admission of the testi-

(Testimony of Otto W. Heider.)

mony of Vern Markee, which is a part of the transcript of the previous hearing. Objection has been made to it. Mr. Dougherty, do you still object to it?

Mr. Dougherty: If the Court please, I have confidence that the Court can extract the relevant parts of it. There are parts that are not particularly relevant to this particular controversy, but we withdraw our objection.

The Referee: All right, then, that will be so understood. Mr. Heider is going to send in a certified photostatic copy of the first mortgage, which will be given an exhibit number. What will the next exhibit number be?

The Reporter: 32, your Honor.

The Referee: And do you desire to introduce copies of any of the complaints—of the first complaint over there?

Mr. Bollenback: We might reserve the right to, your Honor. I don't know if, after further consideration, we will or not, but I think we ought to reserve the right.

The Referee: Well, I think that you have had so much argument about it, I think that it might clear up the record a little if you would submit it.

Mr. Bollenback: Very well, we will put them in.

The Referee: That will be the next exhibit. 32 will be [120] the number of the photostatic copy furnished by Mr. Heider, and 33 will be the complaints in the Circuit Court.

Mr. Bollenback: We can put in all five of them if you want.



(Testimony of Otto W. Heider.)

The Referee: Do you have any objection?

Mr. Dougherty: No, your Honor.

The Referee: All right, you may combine them all.

Then we will adjourn this hearing with the agreement with counsel that later on we desire oral argument, or if Mr. Heider desires to introduce further testimony he may do so, only on that point on that note.

Mr. Heider: Yes, that Long note.

(Witness excused.)

(Hearing adjourned at 4:25 o'clock p.m.,  
March 14, 1956.) [121]

### Reporter's Certificate

I, Lunetta Bussey, hereby certify that on Wednesday, March 14, 1956, I reported in shorthand certain testimony and proceedings had in the above-entitled cause; that I subsequently caused my said shorthand notes to be reduced to typewriting, and that the foregoing transcript, consisting of 121 pages, numbered 1 to 121, both inclusive, constitutes a full, true, and accurate transcript of said testimony and proceedings, so taken by me in shorthand on said date as aforesaid, and of the whole thereof.

Dated this 26th day of April, 1956.

/s/ LUNETTA BUSSEY,  
Court Reporter.

## CERTIFICATE OF CLERK

United States of America,  
District of Oregon—ss.

I, R. DeMott, Clerk of the District Court of the United States for the District of Oregon, do hereby certify that the foregoing documents consisting of Order of General Reference in Judge's Absence; Order of Adjudication; Order Approving Trustee's Bond; Proof of Secured Debt of Otto W. Heider; Trustee's Objections to Proof of Debt of Otto W. Heider; Supplemental Objections to Claim of Otto W. Heider; Motion of Otto W. Heider to Dismiss Objections to Claim; Findings of Fact and Conclusions of Law; Order Denying Claim of Otto W. Heider; Petition for Review; Trustee's Summary of Evidence; Trustee's Memorandum of Authorities; Certificate of Referee on Petition for Review; Order Dated March 28, 1957, Affirming Referee; Notice of Appeal; Bond for Costs on Appeal; Order Extending Time for Filing Record on Appeal; Stipulation; Order Extending Time for Filing Record on Appeal; Designation of Contents of Record on Appeal; and Order to Transmit Exhibits, constitute the record on appeal from an order of said court in a certain bankruptcy cause therein numbered B-29990, In the Matter of Rand Truck Line, Inc., an Oregon corporation, bankrupt, in which Otto W. Heider, a creditor, is the appellant, and Samuel A. McAllister, Trustee in Bankruptcy, is the appellee; that said record has been prepared by me in accordance with

the designation of record on appeal filed by the appellant, and in accordance with the rules of this court.

I further certify that I am sending in addition to the said transcript of record, and under separate cover, two copies of reporters transcript of testimony dated July 6, 1949, and March 14, 1956, together with Trustee's Exhibits No. 1 to No. 19, inclusive, No. 21 to No. 29, inclusive, and No. 33; and Claimants Exhibits No. 20 and No. 30.

I further certify that the cost of filing the notice of appeal is \$5.00 and that the same has been paid by the appellant.

In Testimony Whereof I have hereunto set my hand and affixed the seal of said court in Portland, in said District, this 22nd day of July, 1957.

[Seal]

R. DEMOTT,  
Clerk.

By /s/ E. W. DAVIS,  
Deputy.

[Endorsed]: No. 15646. United States Court of Appeals for the Ninth Circuit. Otto W. Heider, Appellant, vs. Samuel A. McAllister, Trustee in Bankruptcy of the Estate of Rand Truck Line, Inc., Appellee. Transcript of Record. Appeal from the United States District Court for the District of Oregon.

Filed July 23, 1957.

Docketed July 27, 1957.

/s/ PAUL P. O'BRIEN,  
Clerk of the United States Court of Appeals for the  
Ninth Circuit.

In the United States Court of Appeals  
for the Ninth Circuit

No. 15,646

In the Matter of:

RAND TRUCK LINE, INC.,

Bankrupt,

OTTO W. HEIDER, a Creditor,

Appellant,

vs.

S. A. McALLISTER, Trustee in Bankruptcy,

Appellee.

STATEMENT OF POINTS ON  
WHICH APPELLANT RELIES

The points on which appellant intends to rely in this appeal are as follows:

(1) The Bankruptcy Court was without jurisdiction to consider the objections of appellee to the claim of appellant.

(2) Even if the Bankruptcy Court had such jurisdiction, such objections should not have been considered because of undue laches on the part of appellee.

(3) That the order attacked is not, in fact or in law, supported by the findings.

(4) That the findings, material to the claim of appellant, are erroneous and without any support in the record.

/s/ WILLIAM E. DOUGHERTY,  
Of Attorneys for Appellant.

Affidavit of service by mail attached.

[Endorsed]: Filed September 25, 1957.

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[Title of Court of Appeals and Cause.]

MOTION WITH RESPECT TO PRINTING  
OF EXHIBITS AND ORDER

Now comes appellant and respectfully shows the Court that there are in this cause a substantial number of documentary exhibits (including accounting records) which would be very expensive to print or otherwise reproduce, and which may easily be considered in their original form; and

Moves the Court for an order permitting all of said documentary exhibits to be considered by the Court in their original form without the necessity of printing or otherwise reproducing the same.

/s/ WILLIAM E. DOUGHERTY,  
Of Attorneys for Appellant.

So Ordered:

/s/ ALBERT L. STEPHENS,  
Chief Judge, U. S. Court of Appeals for the Ninth  
Circuit.

[Endorsed]: Filed September 25, 1957.

**United States**  
**COURT OF APPEALS**  
**for the Ninth Circuit**

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OTTO W. HEIDER,

*Appellant,*

vs.

SAMUEL A. McALLISTER, Trustee in Bankruptcy  
of the Estate of Rand Truck Lines, Inc.,

*Appellee.*

---

**BRIEF OF APPELLEE**

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*Appeal from the United States District Court for the  
District of Oregon.*

---

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FILED

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PAUL P. O'BRIEN, CLERK





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**United States**  
**COURT OF APPEALS**  
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OTTO W. HEIDER,

*Appellant,*

vs.

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of the Estate of Rand Truck Lines, Inc.,

*Appellee.*

---

**BRIEF OF APPELLEE**

---

*Appeal from the United States District Court for the  
District of Oregon.*

---

**SUPPLEMENTAL STATEMENT OF THE CASE**

Appellee believes that a more complete and accurate statement of the case, than contained in the appellant's brief, would be of material assistance to the court in determining the question of jurisdiction, the only question urged by the appellant.

An order to show cause was issued by the referee before whom the matter was pending, the Honorable Estes Snedecor, requiring the appellant to appear on July 6, 1949, and show cause why certain property of the bankrupt in the possession of the trustee claimed to be subject to a mortgage in appellant's favor, should

not be sold free from liens with the proceeds impressed with such liens as the court should determine to be valid (Referee's Certificate R. 41).

In response to this order the appellant filed his proof of secured claim, with the mortgage and notes attached thereto in the bankruptcy court June 30, 1949 (R. 5-19).

A hearing was had on July 6, 1949, as the result of which an order was entered by the referee, with the consent of the appellant (R. 105-106), authorizing the sale of the tangible assets free from the claim of any mortgage held by appellant and "providing that the proceeds of the sale be impressed with the lien of such mortgage or claimed mortgage, the court expressly reserving the right and power to determine the validity or amount due upon such mortgage" (Referee's Certificate R. 41).

Thereafter such assets were sold and the proceeds collected. The order authorizing the sale provided that the proceeds of the sale should be impressed with the liens found upon the personal property so sold "with this court reserving the power to determine the validity and amount of all such liens" (Referee's Certificate R. 41).

On the same day as the entry of this order, an order was entered authorizing a suit by the trustee, in the state courts, against officers and directors of the bankrupt corporation and Otto W. Heider, appellant herein, for the recovery of certain corporate funds used by such officers and directors and delivered to the appellant in

an attempt to pay personal obligations owing by them to him (R. 41-42).

Such suit was commenced in the Circuit Court of the State of Oregon for the County of Multnomah.

In response to the trustee's Fourth Amended Complaint in this suit the appellant included in his answer a counterclaim seeking to foreclose the identical note and mortgage that is the basis of his claim filed in the bankruptcy court (Ex. 33).

As to the trustee, after alleging his appointment, the appellant alleged:

"The plaintiff herein (trustee) holds funds in his possession belonging to the defendant, Otto W. Heider, which have not been, and should be, applied in payment and in satisfaction of the balance due upon said note and mortgage above described; and the property therein set forth is held as security therefor, and said mortgage is a first and prior and unsatisfied lien against said personal and real property and is unsatisfied."

The prayer asked for a decree determining said mortgage to be a valid and subsisting and prior obligation against the property involved and that the funds in the hands of the plaintiff (trustee) should first be applied in satisfaction thereof and that appellant be allowed attorney fees.

The trustee, in his reply to this counterclaim, pleaded in abatement thereto, that at the time of adjudication in bankruptcy of bankrupt, certain property was owned by it and in its possession; that the trustee took possession of the same and sold it free from liens pursuant to orders of the bankruptcy court; that the trustee had

certain funds in his possession received from the sale of such property as well as other funds; that the appellant had filed a claim in the bankruptcy proceedings for the claimed balance due upon the note and mortgage which claim had not been acted upon but was still pending; that by reason of such bankruptcy proceedings, the exclusive jurisdiction of the United States District Court for the District of Oregon over the funds in the trustee's possession, and the claim of appellant filed in such proceedings, the counterclaim of appellant should be abated and appellant relegated to his rights in the bankruptcy proceedings (Ex. 33), and in his reply to the merits of the alleged counterclaim, the trustee pleaded the defense of usury.

Under Oregon procedure, this reply to the merits of the counterclaim was joined with the plea in abatement. The action in the State court is still pending and the plea in abatement has not been determined.

Thereafter, objections were filed to appellant's claim in the bankruptcy proceedings.

A motion to dismiss such objections was made "on the ground that the bankruptcy court is without jurisdiction to entertain these objections because the same matter has been submitted to the Circuit Court of the State of Oregon for the County of Multnomah. . . ." (R. 29).

This motion was denied. The referee said (R. 155): "The only matter before this court is the validity of his claim and the mortgage securing his alleged claim. I don't think this court can relinquish paramount jurisdiction to determine that matter."

As stated in the referee's certificate (R. 42) he ruled that

"The action in the state court is for the recovery of corporate funds and only indirectly involves the question of the validity of the Heider mortgage."

Upon the hearing, appellant's claim was denied. On appeal to the District Court for Oregon, the referee's decision was affirmed. The appellant then brought his appeal to this court.

## **ON OTHER ISSUES**

We have confined the statement of the case to the jurisdictional question since the appellant is not urging the other specifications of error.

## **STATUTES INVOLVED**

The provisions of the Bankruptcy Act involved in this case are (Title 11, Ch. 2, Sec. 11 USCA):

"Creation of courts of bankruptcy and their jurisdiction:

"(a) The Courts of the United States hereinbefore defined as courts of bankruptcy are hereby created courts of bankruptcy and are hereby invested . . . with such jurisdiction at law and in equity as will enable them to exercise original jurisdiction in proceedings under this title . . . to—

\* \* \*

"(2) Allow claims, disallow claims, reconsider allowed or disallowed claims and allow or disallow them against bankrupt estates;

\* \* \*

“(7) Cause the estates of bankrupts to be collected, reduced to money, and distributed, and determine controversies in relation thereto, except as herein otherwise provided, . . . ”

## **ANSWER TO SPECIFICATION OF ERROR**

The lower court was correct in denying appellant's motion to dismiss on jurisdictional grounds.

## **SUMMARY OF ARGUMENT**

The suit was properly brought in the state courts but that suit was and is separate and distinct from the claim filed by the appellant in the bankruptcy court and the objections filed thereto.

The fact that the trustee will be bound by the decision in the state courts, as to the cause of action being pressed by him in that court, does not have any effect upon the litigation in the bankruptcy court with reference to the claim filed by the appellant.

Authority to commence the state court litigation was not an abdication by the bankruptcy court of its powers and jurisdiction to administer the estate of the bankrupt, and to pass on claims filed in said estate, and the validity of liens upon funds in its possession. Consent of bankruptcy court to action against trustee in state courts can be revoked prior to adjudication.

Allowance and disallowance of claims filed therein, is within the exclusive jurisdiction of the bankruptcy court.



Determination of the validity of liens claimed to exist against property in its possession is within the exclusive jurisdiction of the bankruptcy court.

In this case, the bankruptcy court, by its orders, expressly reserved to itself, the power and right to determine the validity of appellant's lien.

Appellant submitted to the jurisdiction of the bankruptcy court, filed his claim therein, and consented to the sale of the personal property free from the lien of his alleged mortgage. Appellant is bound by the orders of the bankruptcy court reserving the right and power to determine the validity of liens claimed against the property in its possession and cannot oust that jurisdiction by asserting the same claim in the state court proceedings.

## **ARGUMENT**

In the opening portion of his argument, appellant makes numerous statements not in accord with the facts and record. The referee never authorized nor consented to the litigation, in the state courts, of the merits of appellant's claim; the trustee objected to its assertion in that court on the ground that the bankruptcy court had exclusive jurisdiction thereof (Ex. 33) and the referee, in denying the motion to dismiss the objections to appellant's proof of claim did so on the ground that the bankruptcy court had exclusive jurisdiction to pass upon the same (R. 155). The court will recognize other discrepancies.

*Luikart v. Farmers Lumber Co.*, 38 F.2d 588, cited to the effect that a federal court has no power to supervise a state court, is not in point. In that case, an action was commenced in the federal courts to annul and vacate a judgment of the courts of the State of Wyoming. The court refused the relief asked.

### **Answer to Contention That Suit Is Properly Brought in the State Court**

The trustee has no quarrel with the proposition that the suit was properly brought in the state courts and that as to the cause of action set out in his complaint filed therein the state court's adjudication will be final. But that is not the question involved here.

The question for decision is whether the appellant can nullify the proceedings in the bankruptcy court,oust the bankruptcy court of its jurisdiction to pass upon claims filed with it, and of its jurisdiction to determine the validity of liens claimed to exist upon property in its possession, by asserting a counterclaim in the state court litigation.

The authorities cited by appellant recognize the paramount jurisdiction of the bankruptcy court under such circumstances.

The extraordinary relief of mandamus was denied the trustees in *Ex Parte Baldwin*, 291 U.S. 610 (App. Br. 8), but it was pointed out that the trustees could have applied to the bankruptcy court for injunctive relief to restrain action in the state courts. The court said (p. 616):

"The inherent power of the bankruptcy court to protect its jurisdiction, over property of which it has taken possession, from interference by suit thereafter begun in a state court has not been abridged. . . ."

*Herman v. Cullerton*, 13 F.2d 754, 755, quoted by appellant (App. Br. 8) involved a fund paid into the state court, where the trustee appeared and defended. It was held the trustee was bound by the state court judgment, but the court indicated that the result would have been otherwise had the fund been in the possession of the bankruptcy court.

*Thompson v. Magnolia Co.*, 309 U.S. 478 (App. Br. 8), involved oil rights upon railroad right of ways. The court said at p. 483:

"A court of bankruptcy has an *exclusive and non-delegable* control over the administration of an estate in its possession. But the proper exercise of that control may, where the interests of the estate and the parties will best be served, lead the bankruptcy court to consent to submission to state courts of particular controversies involving unsettled questions of state property law and arising in the course of bankruptcy administration."

In the instant case, not only was there no consent by the bankruptcy court to litigation in the state courts of the merits of the appellant's claim to a note and mortgage upon the assets of the bankrupt corporation, but the approval or disapproval of claims is within the "exclusive and non-delegable" jurisdiction of the bankruptcy court.

## **Answer to Contention That the Issues Are Identical**

The issues in the complaint filed by the trustee in the state court were, basically, the transfer of property of the bankrupt in fraud of creditors and conversion thereof by the officers and directors of the bankrupt, and the appellant, Otto W. Heider.

When the alleged counterclaim was asserted, the trustee coupled his plea in abatement raising the question of jurisdiction with an answer to the merits of the alleged counterclaim.

Such procedure is proper under Oregon practice and does not waive the jurisdictional question.

*Credit Service Co. v. Korn*, 121 Or. 685, 256 Pac. 1047.

This answer to the merits, raised the issue of usury as a defense. This is an issue that was not part of the trustee's cause of action as stated in his complaint.

"The defense of usury must be distinguished from the right of action to recover a penalty for usury. Although the defense of usury is personal to a debtor, the right to assert this defense passes to the trustee." *Remington on Bankruptcy*, 5th Ed., Vol. 4, Sec. 1426, p. 136.

Since this defense exists, it was only proper to assert it in the reply to the merits to the alleged counterclaim as well as the objections to appellant's claim.

The referee held that the validity of the Heider mortgage was only indirectly involved in the suit in the state court (Referee's Certificate R. 42). This is true, because had the same transactions occurred, as alleged

in that complaint, without existence of the claimed security asserted by the appellant, or any claimed balance due appellant the trustee's rights to recover the moneys would have been the same.

It probably is proper to say that some of the facts involved in the state court litigation are the same as the facts involved in the appellant's claim filed in the bankruptcy court and objections thereto but the legal issues are different.

### **Answer to Contention That Trustee Is Bound by the State Court Proceedings**

The trustee admits that as to the cause of action set out in his complaint, in the state court proceedings, he will be bound by the result thereof in the state court.

As to the appellant's authorities, *Herman v. Cullerton*, 13 F.2d 754 (App. Br. 9-10), was distinguished *supra*.

*In re American Fidelity Corp.*, 28 F. Supp. 462 (App. Br. 10), involved a litigation commenced prior to bankruptcy over a fund and the court pointed out that it was questionable whether the bankruptcy court had either actual or constructive possession thereof. The trustee, with the bankruptcy court's permission intervened, and the judgment of the state court was binding upon him. The court recognized that there was certain functions of the bankruptcy court which are non-delegable (p. 468):

"Nor does it question that there are certain administrative functions which by their very nature are not capable of delegation."

In *Van Zandt v. Parson*, 81 Or. 453, 456, 159 Pac.

153 (App. Br. 10), the same general rule is applied. When a trustee sues in a state court, he is bound by the adjudication; the question of the right of the bankruptcy court to pass on claims filed with it or determine liens upon funds in its possession were not involved.

In *Grant v. Buckner*, 172 U.S. 232, 238 (App. Br. 10), the court pointed out:

"The question presented is not how the estate belonging to the receiver shall be administered, but what is the estate belonging to him."

Applying this test to the present case, the complaint filed by the trustee in the state court involves "what is the estate" belonging to the trustee, while the counter-claim attempted to be asserted attempts to deprive the bankruptcy court of jurisdiction to determine "how the estate . . . shall be administered."

*Winchester v. Heiskell*, 119 U.S. 450, and *Fischer v. Pauline Oil Co.*, 309 U.S. 294, 303 (App. Br. 10), both apply the rule of the previous cases cited; as stated in *Crown v. Gerdes*, 321 U.S. 178, at pp. 185, 186:

"A bankruptcy trustee who by choice or by necessity resorts to a state court for the prosecution of a claim is of course bound by the adjudication made in the state proceeding. *Winchester v. Heiskell*, 119 US 450; *Fischer v. Pauline Oil & Gas Co.*, 309 US 294, 303. The state court has full control over the litigation. *But even as an incident thereto, it may not take action which involves the performance of functions which Congress has entrusted to the bankruptcy court.* See *Eau Claire National Bank v. Jackman*, 204 U.S. 522, 537-538."

and in the quoted case, *Eau Claire National Bank v. Jackman*, *supra*, the court said:

"The bank also contends, in effect, that in such suit (to recover a preference) the validity of all other claims against the bankrupt can be litigated and whether they have received voidable preferences and have not been required to surrender them. The broad effect of the contention repels it as unsound. To yield to it would transfer the administration of a bankrupt's estate from the United States District Court to the state court."

### **Answer to the Contention That the Principle Is Still Applicable Where the State Court Has Not Yet Rendered Judgment**

This contention is not correct. The cases cited do not support it.

*In re Graceland*, 73 F. Supp. 158, 161 (App. Br. 10), was a case where the trustee was expressly directed to try the title to property in the state courts and he instituted action for that purpose. Another action was commenced for the same purpose by others and the trustee intervened as a party defendant. The question was whether prosecution of the second action should be enjoined. The court said:

"Since the trustee was directed to try title in the state court, he cannot object that this result may be attained by means of the . . . cross complaint . . . rather than in his own action . . ."

These being the facts, this case is of no help in the matter before this court.

*Scott v. Kelly*, 22 Wall. (89 U.S.) 57, 59 (App. Br. 11), did not involve a pending action, but is another example of the proposition running through all the authorities cited by the appellant—that when a trustee in bank-

ruptcy secures authority to and does submit to the jurisdiction of a state court for the adjudication of a specific issue, that adjudication is binding upon the trustee and the matter cannot be re-litigated in the bankruptcy court.

Until there has been an adjudication, leave to sue can be withdrawn.

In *Investment Registry Ltd. v. C & M Elec. Ry. Co.* (CCA Wisc.), 251 Fed. 510, an Order had been entered authorizing suit against a receiver in the state court. Thereafter a motion to vacate that Order was filed. The court said, at page 512:

"If at any stage of the proceedings the court deems it proper and advisable that any demand or question be litigated elsewhere than in the federal court, it can authorize such litigation to be elsewhere instituted. But neither on principle nor authority does it follow that the court granting the leave to sue may not recall it, if before adjudication in such other tribunal the court granting the leave shall consider, either because of facts subsequently arising, or of new light coming to it as to then existing conditions, it would best subserve the due administration of the estate to recall the granted leave,"

and at page 513:

"If it appeared that any issue in the litigation had been determined by the state court in which the action was brought, pursuant to the leave granted, a different question might be presented."

And in *In re Locust Building Co.*, 272 Fed. 988, aff'd 76 Fed. 1023 (CCANY), a third mortgagee had obtained from the bankruptcy court leave to foreclose his mortgage in the state courts; the trustee had been directed by Order to sell the property covered by the



mortgage and to pay the mortgages (so far as held valid) out of the proceeds.

Thereafter, upon motion, the court stayed the foreclosure proceedings. The court said (272 Fed. at 989):

“If the state court did not deem it advisable or was unable to proceed with the liquidation of this claim and the determination of its validity within a reasonable time, the trustee could nevertheless in due course proceed before the referee or this court to determine how the fund should be distributed. . . .”

It is the trustee's position that the bankruptcy court reserved to itself the right to determine the validity of appellant's lien but if any consent to assert this lien in the state court be implied from the granting of the authority to bring the state court action, such consent was revoked or cancelled by the denial of the motion to dismiss on jurisdictional grounds.

### **The Bankruptcy Court Has Exclusive Jurisdiction to Pass on Claims Filed With It**

The question for decision in this case is—does a trustee by going into the state court for the recovery of assets belonging to the bankrupt estate, thereby subject the assets of that estate to the jurisdiction of the state court so that the state court can pass on claims, determine the validity of liens upon funds in the custody of the bankruptcy court and thereby oust the jurisdiction of the bankruptcy court from the administration of the estate and the assets in its possession. The answer is clearly no—the state court's jurisdiction is limited to the controversy submitted to it and it cannot infringe

upon the other functions of the administration of the estate which are within the exclusive jurisdiction of the bankruptcy court.

The bankruptcy court has exclusive and non-delegable jurisdiction to pass on claims filed with it.

The United States Supreme Court in *Pepper v. Litton*, 308 U.S. 295, 304, said:

"Among the granted powers are the allowance and disallowance of claims; the collection and distribution of the estates of bankrupts and the determination of controversies in relation thereto; the rejection in whole or in part 'according to the equities of the case' of claims previously allowed; and the entering of such judgments 'as may be necessary for the enforcement of the provisions' of the act. In such respects the jurisdiction of the bankruptcy court is exclusive of all other courts. *United States Fidelity & Guaranty Co. v. Bray*, 225 U.S. 205, 217."

In the cited case of *United States Fidelity & Guaranty Co. v. Bray*, supra, the United States Supreme Court, after citing Sections 2, 23(a) and 57(k), states the following:

"We think it is a necessary conclusion from these and other provisions of the Act that the jurisdiction of the bankruptcy courts in all 'proceedings in bankruptcy' is intended to be exclusive of all other courts, and that such proceedings include, among others, all matters of administration, such as the allowance, rejection and reconsideration of claims, the reduction of the estates to money and its distribution, the determination of the preferences and priorities to be accorded to claims presented for allowance and payment in regular course, and the supervision and control of the trustees and others who are employed to assist them."

The court in the last cited case further stated the following (p. 218):

“Of the fact that the suit was begun in the Circuit Court with the express leave of the court of bankruptcy it suffices to say that the latter was not at liberty to surrender its exclusive control over matters of administration or to confide them to another tribunal.”

Remington on Bankruptcy, 5th Ed., Vol. 5, Sec. 2369, p. 569:

“In general, neither a State Court, nor the United States District Court, has jurisdiction, even by express permission of the bankruptcy court, to maintain an action the object of which is to determine the validity or extent of a claim against a bankrupt estate that is in process of administration in the Bankruptcy Court, or to determine priorities in the distribution of the assets of a bankrupt estate in such custody; for the jurisdiction of the Bankruptcy Court over the administration of the bankrupt estate is original and exclusive; and the Bankruptcy Court has no authority to delegate that jurisdiction to another court.”

To the same effect, see Collier on Bankruptcy, 14th Ed., Vol. 3, Par. 57.14, p. 185.

**The Property Being in the Custody of the  
Bankruptcy Court, Its Jurisdiction to  
Determine the Validity of Liens  
on the Property Is Exclusive**

In *Isaacs v. Hobbs Tie & Timber Co.*, 282 U.S. 734, the court said at pp. 737-738:

“Upon adjudication, title to the bankrupt’s property vests in the trustee with actual or constructive possession, and is placed in the custody of the bank-

ruptcy court. *Mueller v. Nugent*, 184 US 1, 14. The title and right to possession of all property owned and possessed by the bankrupt vests in the trustee as of the date of the filing of the petition in bankruptcy, no matter whether situated within or without the district in which the court sits (citing cases). It follows that the bankruptcy court has exclusive jurisdiction to deal with the property of the bankrupt estate. . . . When this jurisdiction has attached the court's possession cannot be affected by actions brought in other courts. *White v. Schloerb*, 178 US 542; *Murphy v. Hofman Co.*, 211 US 562; *Dayton v. Stanard*, 241 US 588. This is but an application of the well recognized rule that when a court of competent jurisdiction takes possession of property through its officers, this withdraws the property from the jurisdiction of all other courts which, though of concurrent jurisdiction, may not disturb that possession; and that the court originally acquiring jurisdiction is competent to hear and determine all questions respecting title, possession and control of the property. *Murphy v. Hofman Co.*, supra; *Wabash R. Co. v. Adelbert College*, 208 US 38; *Harkin v. Brundage*, 276 US 36. Thus, while valid liens existing at the time of the commencement of a bankruptcy proceeding are preserved, it is solely within the power of a court of bankruptcy to ascertain their validity and amount and to decree the method of their liquidation. *Ex parte City Bank of New Orleans*, 3 How 292; *Houston v. City Bank of New Orleans*, 6 How 486; *Ray v. Norseworthy*, 23 Wall 128; *In re Wilka*, supra; *Nisbet v. Federal Title & T. Co.*, 229 Fed 644. The exercise of this function necessarily forbids interference with it by foreclosure proceedings in other courts, which save for the bankruptcy proceeding would be competent to that end. . . ."

(P. 739):

" . . . The jurisdiction in bankruptcy is made exclusive in the interest of the administration of the

estate and the preservation of the rights of both secured and unsecured creditors. This fact places it beyond the power of the court's officers to oust it by surrender of the property which has come into its possession. *Whitney v. Wenman*, 198 US 539; *In re Schermerhorn*, 145 Fed. 341. Indeed a court of bankruptcy itself is powerless to surrender its control of the administration of the estate. *U. S. Fidelity & G. Co. v. Bray*, 225 US 205. The action of the trustee in removing the cause, could not, therefore, divest the Texas District Court of its jurisdiction. . . ."

See also *Irving Trust Co. v. Fleming* (CCA 4th Cir.), 73 F.2d 423 at 427.

### **Having Filed His Claim Appellant Is Subject to Jurisdiction of Bankruptcy Court**

In *Gardner, Trustee, v. New Jersey*, 329 U.S. 565, the court said:

"It is traditional bankruptcy law that he who invokes the aid of the bankruptcy court by offering a proof of claim and demanding its allowance must abide the consequences of that procedure. *Wiswall v. Campbell*, 93 US 347, 351."

See also *In re McCallum* (DC ED Pa.), 113 Fed. 393.

### **CONCLUSION**

It is respectfully submitted that the lower court must be affirmed.

Respectfully submitted,

C. X. BOLLENBACK,  
F. BROCK MILLER,  
Attorneys for Appellee.

